The State of Small Business

Ontario

1989

Annual Report on Small Business in Ontario

MINISTRY OF INDUSTRY, TRADE AND TECHNOLOGY

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Minister of Industry, Trade and Technology

It is with pleasure that I present the fourth annual report on The State of Small Business in Ontario. The contribution that small businesses make to our economy is once again highlighted in this edition through the data and new research findings.

I am grateful for the work of my former Parliamentary Assistant and Small Business Advocate, Mr. Steven Mahoney, M.P.P., and his colleagues on the Committee of Parliamentary Assistants for Small Business.

Mr. Douglas Carrothers, M.P.P., my new Parliamentary Assistant, who is Small Business Advocate, now chairs the Committee of Parliamentary Assistants for Small Business and will be continuing its worthwhile activities.

Over the next year, this Ministry will be looking to the future of entrepreneurship by emphasizing the importance of youth and education. Visions, a program to bring entrepreneurs into the classroom, will be starting in 1990. As well, many secondary schools will offer a new course in entrepreneurship. I know students and teachers will find this report a useful aid, bringing current information and relevant business issues into the educational system.

Monte Kwinter
Minister

The Honourable Monte Kwinter
Minister
Ministry of Industry, Trade and Technology
8th Floor, Hearst Block
Queen's Park
Toronto, Ontario

Dear Mr. Minister:

It is my privilege to present to you the fourth annual report on The State of Small Business, prepared during my tenure as your Parliamentary Assistant and the Small Business Advocate for Ontario.

The 1989 report focuses on the world of the entrepreneur and includes a section on people employed in small businesses. The importance of small business to our changing economy is once again clearly evident in new research findings.

I wish every success to your new Parliamentary Assistant, Mr. Douglas Carrothers, M.P.P., as the new Small Business Advocate and Chairman of the Committee of Parliamentary Assistants for Small Business.

On behalf of the outgoing committee and myself, I thank you and your Ministry staff for the dedicated support we received.

Yours sincerely,

Steven W. Mahoney, M.P.P.

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The project was designed and written by Donald Rumball in co-operation with Rena Blatt, Research Advisor in the Small Business Branch of the Ministry of Industry, Trade & Technology. Other members of the staff of the Small Business Branch also contributed significantly, especially Jeffrey Stutz, Manager of Small Business Advocacy and Geoffrey Hale, Small Business Advocate.

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Statistics Canada,

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Sharon Hall,
Bill Lampert,
Elli Murack.

THE STATE OF SMALL BUSINESS ONTARIO, 1989 SUMMARY

PART I

The World of the Entrepreneur

Ontario is Canada's most entrepreneurial province. In 1986, 408,000 Ontarians were self-employed. That's 8.3% of the workforce. It's also about 34% of the 1,209,000 self-employed in the whole country.

The number of new business starts at the end of this decade has risen to half as much again as the number at the end of the 1970s. Between 1981 and 1986, the number of self-employed Ontarians grew by 14%.

Self-employed people earn almost 50% more, on average, than employees.

Start-ups

Ten years after start-up, only a quarter of new businesses are still operating. Almost half of them go under in the first three years. There is a core of businesses that are long-term successes, but the average life of all small business is only 7 years.

About a half of all new ventures are incorporated. One-third of them incorporate immediately on start-up and the rest do so within three years.

Owners of incorporated firms invest more, they have higher expectations of growth and they employ more people. Their companies also generate much higher earnings for their owners, who take home a third more than owners of unincorporated businesses.

Only one-half of the owners of new ventures have direct or related experience in the field they are entering. By contrast, up to the 1981-82 recession, 60% had experience running a business and about 80% had relevant experience in the field of their new business.

About half of the owners of new ventures expect to grow to

become big companies. Half of them prepare business plans, compared to one-third of the people who do not expect to grow big.

Half of all new ventures now are started without borrowing a cent. Only one-eighth of new unincorporated businesses raise equity financing and just more than a third borrow from the banks. About 30% comes from their own pockets and the rest is "love money" from their relatives and friends. The average investment to start a new business now is less than $50,000. More than a half of all start-ups have less than $15,000 invested in them.

Half of the people who go into business for themselves run their new firms from their homes and 42% keep their jobs as employees, running their businesses part-time until they build it up to the point where they can quit and become full-fledged entrepreneurs.

Demographics

The average age of self-employed people is 44, compared to 36 for employees. There are young entrepreneurs, of course, but only 4% of the self-employed are younger than 25, compared to 23% of the whole labour force. Self-employed people aged 35-44 account for 29% of the total, compared to 22% of employees.

These young self-employed people are much better educated than their predecessors. Less than a half of the self-employed people over 45 have post-secondary education, compared to almost two-thirds of those under 45.

Entrepreneurs with post-secondary education earn almost 20% more than the average income for all entrepreneurs. The rest earn less than 80% of the average .

Motivation

The top six motivations of people starting a business are:

- The need to achieve;
- The need to be their own boss;
- A perceived opportunity in the marketplace;
- The wish to do things their own way;
- The adventure of independence; and
- The money.

Once they have established themselves, the top six motivations of successful entrepreneurs are:

- Having fun;
- Building an organization;
- Money;
- Winning in business;
- Recognition; and
- A sense of accomplishment.

Strategy and Information Needs

When they start their businesses, new entrepreneurs need lots of specific advice, so they seek out professionals, bankers and people in the same business. Once they mature and become established, however, they need a different kind of information, such as intelligence about the strategies of competitors, discontinuities in the economy and technological breakthroughs. Often they don't even know if the information they're looking for exists at all. So they develop antennae, mainly by reading and developing personal networks, so that they can at least become aware of what information they should be trying to acquire.

About a half of successful entrepreneurs read an hour or more a day. Three-quarters make a special effort to build a personal network. Unlike the people in start-ups, these people spend most of their time with businesspeople, often in unrelated businesses, who can offer insights into the opportunities and problems in their own industry. Their next most popular contacts in their networks are customers, government people and their own suppliers. Professionals are last.

Only 40% of established entrepreneurs have an active board of directors.

Women

Women are acquiring a higher profile as self-employed people. They now account for about half of the increase in the self-employed. However, only 4.5% of the female labour force are self-employed, compared to 11.25% of men. Still, women now represent almost a quarter of all self-employed people in Ontario and Canada.

When they start a business, women have lower expecta-

tions. They invest less of their money and time in it until they are sure it will fly. Men are more inclined to go for rapid growth immediately. Women accordingly fail less and they earn much less. Women with unincorporated businesses earn less than half what men earn in unincorporated businesses. However, women with incorporated businesses earn 60% of the earnings of men with incorporated businesses.

PART II

The Economic Impact of Small Business

Small firms are the frontrunners in job creation. At the end of the 1970s, they accounted for about half the new jobs. By 1987, firms with fewer than 100 employees accounted for 90% of the new jobs in Canada, 75% in Ontario.

Between 1978 and 1987, small firms in Ontario increased their employment by 69%, compared to 50% elsewhere in Canada and 10% in Ontarian big firms. A small group of 1,500 firms (0.72% of all firms) that grew particularly fast accounted for 20% of all new jobs created in the province between 1978 and 1987.

Firms with fewer than 100 employees now employ 33% of total labour force, or 39% of the private-sector workers. Across Canada, in the private sector, small firms now employ more people than the big firms with more than 500 employees.

New ventures accounted for about 95% of the new jobs created in Ontario during 1978-87.

More than 90% of the province's 300,000-odd firms employ fewer than 20 people and their average number of employees is 4.4. The average size of all of Ontario's firms has fallen three percentage points in the past nine years, to 15 employees per firm. If governments and their agencies are excluded, the average firm size is only 13. (In the rest of Canada, it's nine.)

The big stars of job creation are personal and business services, community services and retail trade. These three together accounted for 60% of the new jobs in Ontario between 1978 and 1987. The power behind these are two stellar industries — services to business and health and welfare. The former is growing at 7% a year in Ontario, far outpacing any other industry.

PART III

The role of Government in Small Business
The Ontario government decided to address start-ups as a mass market, starting in 1984-85, and has put in place well-developed start-up assistance. The Ontario government also created the advocacy program to run interference for beleaguered small businesses when other ministries propose laws or regulations that affect them. The Ontario government also embarked on a series of studies to divine what makes entrepreneurs successful. Programs like the Small Business Development Corporations in the early 1980s and New Ventures in the later 1980s made a solid contribution to promoting entrepreneurship. With an average start-up investment of slightly more than $13,000, New Ventures is developing grass roots entrepreneurship. The Ontario government's counselling program is also providing expert advice in navigating the regulatory and management shoals threatening new and growing businesses.

This phase of government initiative is maturing now. SBDCs have levelled off, although New Ventures is just gathering momentum. With business self-help offices in place across the province, the government is ready to implement new initiatives, both before and beyond the start-up phase.

One step behind the start-up is the informal investor network, the "angels" who fund new entrepreneurs before they reach the stage when they can draw on commercial financing. Before even that stage, the Ontario government is deeply engaged in developing entrepreneurial options for the high-school system. With an experimental new curriculum on entrepreneurship being developed in high schools now and other programs to bring entrepreneurs into the classrooms, young Ontarians are being given an opportunity to appreciate the life of an entrepreneur.

The major needs of small firms at the beginning of the 1990s are in advanced management skills, in dealing with people and in developing management systems to absorb the mounting flow of raw information. There is a role for government to develop an appreciation in small firms of the need for these skills. Effective government programs will help them understand the value of these skills, thereby opening the door

to the private sector to deliver these services at higher, commercially viable rates. For example, the government has introduced a program, called Technical Personnel Program, that will help small firms hire the technical expertise they need to enable their operations to compete effectively abroad.

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PART I

The World of the Entrepreneur

CHAPTER 1
ENTREPRENEURS

In the course of the past decade, there has been a remarkable shift in people's attitudes toward earning a living. One of the more powerful trends is the surging growth in self-employment. Entrepreneurship has long been admired as an economic force. Now it is acquiring enough social cachet to release many of the constraints that have kept potential entrepreneurs working for other people.

Ontario leads Canada in the rate of increase in the self-employed, although the rest of the country still has a higher proportion of self-employed people in the labour force. In 1986, 408,000 Ontarians were self-employed, up 14% from 1981. The self-employed now account for 8.3% of the workforce in Ontario. Almost 34% of the 1.2 million self-employed people in Canada work in Ontario.

The increase in the number of self-employed people is pushing the rate of new business formations to new heights. The number of new business starts at the end of this decade has risen to half as much again as the number at the end of the 1970s.

There are many reasons for this, among them the following:

- Job security in big businesses is more elusive than it has ever been. People who don't fit are more likely to be laid off now — and that includes very capable people who are square pegs in round holes. Many other employees are becoming dissatisfied with life in big organizations. Either way, more and more people, at all levels of big organizations, are turning to self-employment.
- At the same time, the downsizing by big firms has created many opportunities for sub-contracting. People who may once have worked for big companies are now suppliers of services or products to their former employers.
- It's easier to become an entrepreneur now, because most of the growth in the economy is in services, and it costs much less to start a firm in the service industry than it does in manufacturing.

- Self-employed people earn almost 50% more, on average, than employees.

Taking the decision to go on their own, however, is only the first step. The initiation into self-employment can be arduous and expensive. Some of them fail. Others decide it isn't worth it and fold their businesses. Ten years after start-up, only a quarter of new businesses are still operating. Almost half of them go under in the first three years. There is a core of businesses that are long-term successes, but the average life of all small business is only seven years.

This is not as serious as it may seem. Many of the failures are part of the learning curve of new entrepreneurs who may fail in two or three ventures before they establish themselves as successful businesspeople. So the turnover in businesses may be high, but the number of self-employed people grows steadily.

About a half of all new ventures are incorporated. One-third of them incorporate immediately on start-up and the rest do so within three years. There is an important distinction between the two classes of business. Owners of incorporated firms are generally more serious about making their businesses grow. They invest more, they have higher expectations of growth and they employ more people. They are also more professional in their preparation for the start-up. It shows in their results. Their companies grow much faster than unincorporated businesses and generate much higher earnings for their owners, who take home a third more than owners of unincorporated businesses.

* * *

The higher overall level of start-ups has its drawbacks. People now are prepared to embark on new ventures with relatively little experience or money. Only one-half of the owners of new ventures have direct or related experience in the field they are entering. Up to the 1981-82 recession, 60% had experience running a business and about 80% had relevant experience in the field of their new business.

This may not be a problem if the new entrepreneurs have limited expectations for their businesses. Many turn to self-employment to meet lifestyle needs and don't want to grow big. But about half of the owners of new ventures expect to

grow big companies. These people lack experience too, but they prepare for their ventures more carefully. Half of them prepare business plans, compared to one-third of the people who do not expect to grow big. This is more thorough preparation than was the case just ten years ago, thanks mainly to lenders and investors, who demand business plans from putative entrepreneurs these days.

Then again, a lot don't raise much money, particularly if they dip their toes into self-employment rather than plunge in head first. Half of all new ventures now are started without borrowing a cent. Only one-eighth of new unincorporated businesses raise equity financing and just more than a third borrow from the banks. About 30% comes from their own pockets and the rest is "love money" from their relatives and friends. The average investment to start a new business now is less than $50,000. More than a half of all start-ups have less than $15,000 invested in them.

The other side of this coin is that newly self-employed people are more cautious. They understand they have to feel their way first. Half of them run their new firms from their homes and 42% keep their jobs as employees, running their businesses part-time until they build it up to the point where they can quit and become full-fledged entrepreneurs.

Even if they are not experienced in business, entrepreneurs need to be experienced in life. They have to have enormous strength of character and they have to be able leaders. These characteristics are less common in young people than in those with more experience. Indeed, the average age of self-employed people is 44, compared to 36 for employees. There are young entrepreneurs, of course, but only 4% of the self-employed are younger than 25, compared to 23% of the whole labour force. The young people become a far greater force when they reach 35. People aged 35-44 dominate the ranks of the self-employed, accounting for 29% of the total. Only 22% of employees are aged 35-44.

These young self-employed people are much better educated than their predecessors. Less than a half of the self-employed people over 45 have post-secondary education, compared to almost two-thirds of the under 45s. This is not an academic point. Entrepreneurs with post-secondary education earn almost 20% more than the average income, while

the rest earn more than 20% less.

* * *

The motivations that drive these people to subject themselves to the hard labour and heartache of starting a new business are mostly related to wanting the freedom to do things their way, although there is a tinge of business acumen to give it some form. The top six motivations of people starting a business are:

- The need to achieve;
- The need to be their own boss;
- A perceived opportunity in the marketplace;
- The wish to do things their own way;
- The adventure of independence; and
- The money.

Many deny the last motivation, because they are concerned that people will think badly of them or they'll seem to be greedy. But, when entrepreneurs are interviewed intensively, most of them will admit to being motivated by money. They work so hard, they deserve it.

Once they have established themselves, the motivations change, naturally. Being your own boss and doing things your own way are motivating only when you are not your own boss. The top six motivations of successful entrepreneurs are:

- Having fun;
- Building an organization;
- Money;
- Winning in business;
- Recognition; and
- A sense of accomplishment.

* * *

One of the biggest challenges for entrepreneurs is gathering all the information they need. The bureaucracies of big business and government are expert in this task, but entrepreneurs seldom have the time to collect all the information they need. This means some of their decisions are based on questionable information, but they compensate with a marvellous intuition based on their broad-based knowledge of their business.

When they start their businesses, they need lots of specific advice, so they spend most of their free time with

professionals, bankers and people in the same business. Once they mature and become established, however, they start looking around at opportunities for expansion. This creates a demand for a different kind of information — intelligence about the strategies of competitors, discontinuities in the economy, technological breakthroughs and so on. Often they don't even know if the information they're looking for exists at all. The answer is to develop antennae, mainly by reading and developing personal networks, so that they can at least become aware of what information they should be trying to acquire.

About a half of successful entrepreneurs read an hour or more a day. Three-quarters make a special effort to build a personal network. Unlike the people in start-ups, these people spend most of their time with businesspeople, often in unrelated businesses, who can offer insights into the opportunities and problems in their own industry. Their next most popular contacts in their networks are customers, government people and their own suppliers. Professionals are last.

One of the most useful forms of networking is an active board of directors, but only 40% of established entrepreneurs have them. Too many entrepreneurs think they come up with all the good ideas for their businesses, so they don't feel it's necessary to bother with outside directors, who may start "meddling" in the firm's affairs. This can become a weakness.

Another significant potential weakness lies in the internal management of entrepreneurial firms. Few business owners place a high priority on human resource management. When they have problems recruiting and retaining good employees, many of them blame the economic environment, the education system or the local vocational training facilities. Sometimes they are right, but often their problems reflect their neglect, a few years previously, of human resource management.

When their firms are small and still struggling to survive, business owners cannot afford to spend too much time stroking their employees. The employees understand this, too. As the firm grows, however, the owner has to make the transition from a supervisor who makes all the decisions to a leader who lets employees make their own decisions. This makes it more dangerous to ignore human resource manage-

ment. Once firms reach 50 to 75 employees, the need for it becomes obvious and most of them respond. But for firms with 10 to 50 employees, the need is less obvious to extremely busy owners and they frequently don't bother, giving human resource management a low priority. This represents an important gap in the management skills of Ontario small businesses.

* * *

One aspect of all the current trends in self-employment is the growing role of women, who account for about half of the increase in the self-employed. However, it has still not taken hold among women to the same degree it has among men, 11% of whom are self-employed, compared to 4.5% of women. Still, women now represent almost a quarter of all self-employed people in Ontario and Canada, and they are changing the culture of entrepreneurship.

A much higher proportion of women than of men have unincorporated businesses. And most of the people who are running their businesses part-time and/or out of their homes are women. Both these facts reflect their more cautious approach. When they start a business, women have lower expectations of where they'll go with it and they accordingly invest less of their money and time in it until they are sure it will fly. They prefer to test a business idea with minimal investment before they take the plunge and go after significant growth. Men are more inclined to go for rapid growth from the word go, making a bigger investment in cash and in their egos. There are two consequences in all this for women. They fail less and they earn much less. Women with unincorporated businesses earn less than half what men earn in unincorporated businesses.

It is likely that, as women become more accustomed to self-employment, they will start being more adventurous. A strong indication comes from the women who have incorporated their businesses. They earn 60% of the earnings of men with incorporated businesses — a higher ratio than women enjoy among all employees and much higher than among the unincorporated self-employed, of course. Because they are newer to the game and own smaller companies, it's not surprising that they should earn less. For the moment.

THE SMALL BUSINESS FACT SHEET

Number of firms, 1986	Ontario	Canada
Total	290,260	851,492
In small firms	284,066	840,694
Small firms as a percentage of total	97.9%	98.7%

Increase in number of firms, 1978-1986		
Total	74,737	250,664
Small firms as a percentage of total	98.9%	99.3%
Average growth rate p.a. for big firms	1.9%	2.1%
Average growth rate p.a. for small firms	3.8%	4.5%

Number of jobs, 1986		
Total (000s)	4,381.6	10,776.1
In small firms (000s)	1,456.7	3,904.1
Small firms as a percentage of total	33.2%	36.2%

Net gain in jobs, 1978-1987		
Total (000s)	1,021.1	2,042.9
Total percentage increase over period	29%	22%
In small firms (000s)	765.7	1,736.3
Percentage increase in small firms	69%	57%
Share of small firms in net increase	75%	85%
Average growth rate p.a. in big firms	1.1%	0.5%
Average growth rate p.a. in small firms	6%	5%

The big winners		
Share of total employment growth in:		
Personal and business services	28%	31%
Community services	16%	21%
Retail trade	16%	19%
Small-business share of employment growth in:		
Personal and business services	75%	81%
Community services	42%	48%
Retail trade	73%	78%

The self-employed		
Number of self-employed people, 1986	408	1,209
Percentage who are women	24%	22%
Percentage aged less than 25: self-employed	4%	4%
employees	23%	23%

Increase in self-employed, 1981-86		
Total (000's)	50	114
Percentage increase	14%	10%
Increase in self-employed women	27%	27%
Increase in self-employed men	10%	6%

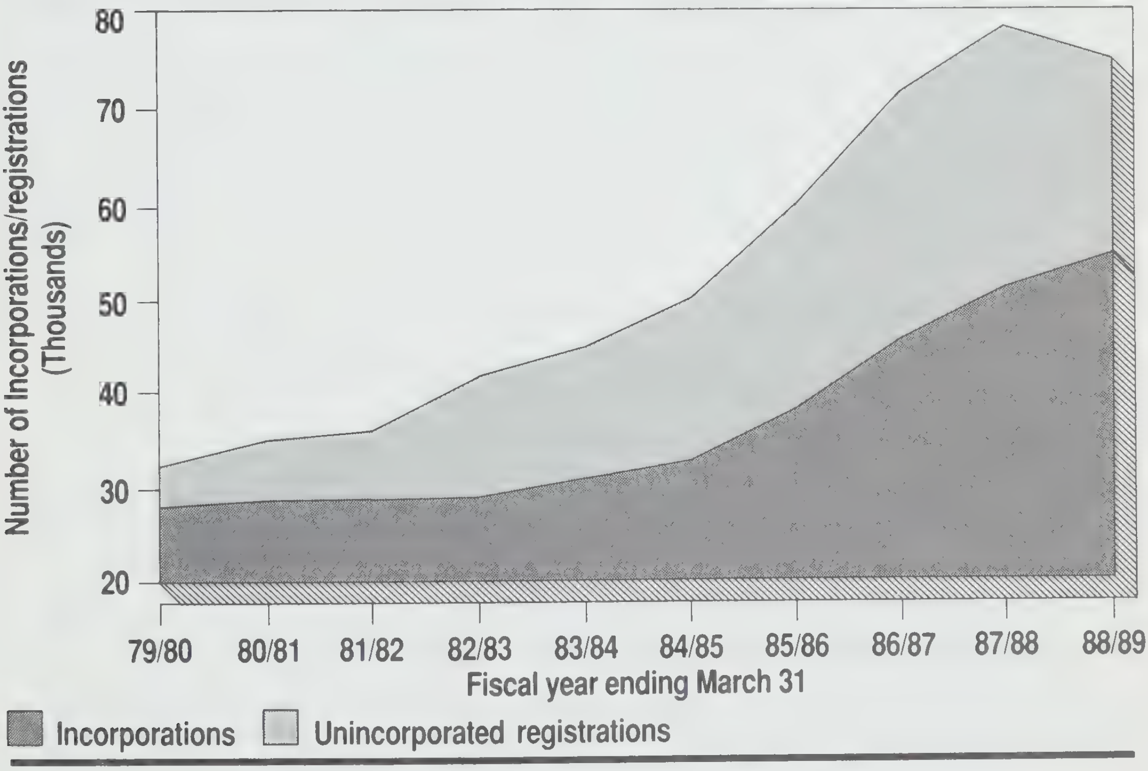
Source: Statistics Canada, Business Microdata Integration and Analysis, Small Business & Special Surveys and 1986 Census.

CHAPTER 2
THE START-UP REVOLUTION

An unexpected dividend of the 1981-82 recession, which wreaked so much devastation on all levels of business in Ontario, has been the subsequent, remarkable surge in new business formations. It started in 1982, when the number of registrations of unincorporated companies jumped sharply, then continued rising, as it doubled within five years. Incorporations started rising rapidly about three years later, as Chart 2.1 shows, and also appear to be doubling in the five years following the initial surge.

Chart 2.1[1]
The Explosion of Start-up Activity

Annual registrations of unincorporated businesses and incorporations in Ontario, 1979-89



[1] Internal research, Ministry of Industry, Trade & Technology, based on data from the Ministry of Consumer and Commercial Relations

The fall in registrations of unincorporated businesses in 1988-89 probably reflects the significant increase in the registration fee, but it may also reflect a period of consolidation as the surge in start-up activity matures into the operation of established firms.

These statistics give an accurate impression of the amount of activity surrounding business start-ups. They are less reliable in measuring the actual number of new businesses started in any one year. They suffer from significant overcounting for a number of reasons. Many incorporations are made by existing unincorporated businesses, or parts of existing businesses. Also, both incorporations and registrations of unincorporated businesses often do not reflect business formations in the year of incorporation or registration. Many people register businesses with the intent of starting a business later and others register even though their businesses have been active for many years.

A recent study of start-ups for the federal government[2] examined 1,731 incorporations and registrations of new businesses in 1987 and found that only 59% of them actually started a business in 1987. 21% had started their businesses between 1970 and 1986, another 14% started in 1988 and 6% did not say when they started operations. When the survey was conducted, in the fall of 1988, 8% of them had not yet started operations and 4% had no idea when they would start, if ever.

The statistics used above and in previous issues of *The State of Small Business* are adjusted to compensate for this overcounting, but the best indication of actual start-ups probably comes from the statistics in the Business Microdata Integration and Analysis, produced by Statistics Canada. Even these statistics are not ideal, however. They count only those firms that employ one or more people. Self-employed people and their partners who do not employ anyone, as well as unpaid family workers are left out. These omissions account for about 10% of total employment and 3% of total payroll income. On the other hand, these statistics overstate

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[2] *Study of Business Start-ups in Canada*, Decision Marketing Research Limited, 1988

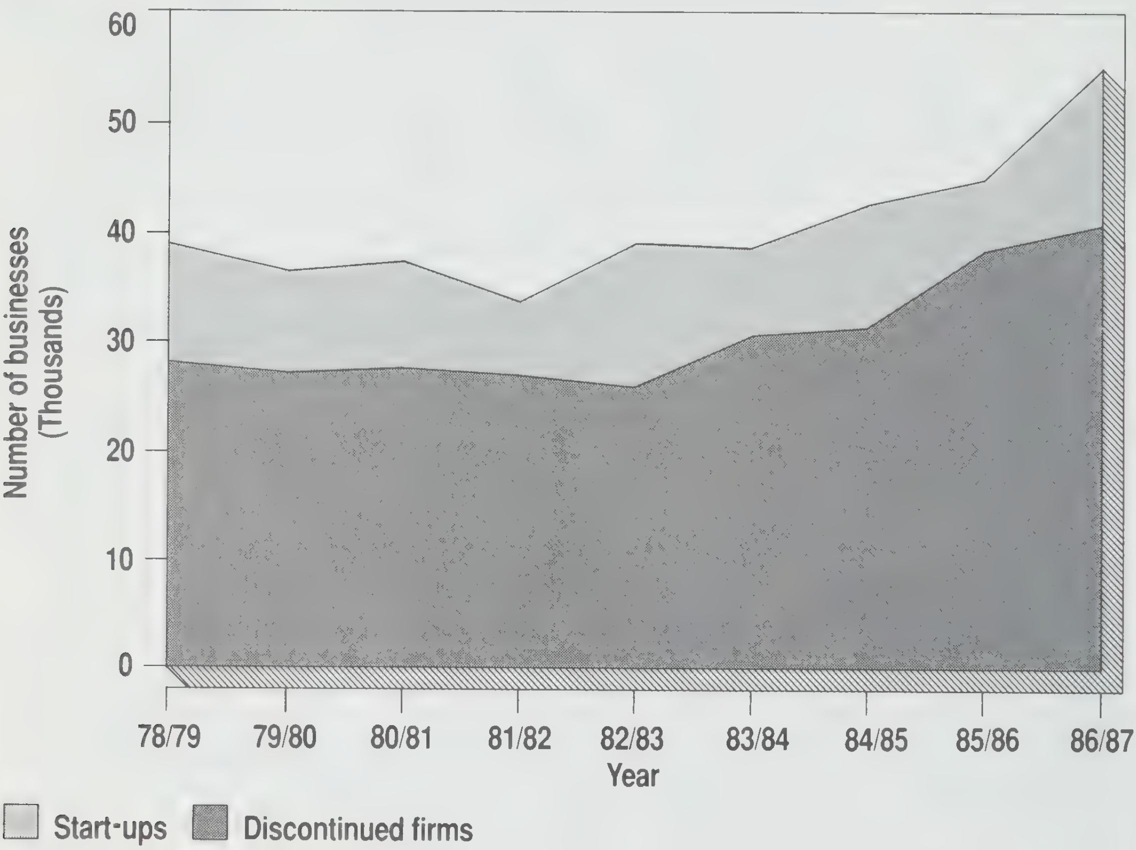
the real numbers because some of the "new" firms are corporate reorganizations of existing businesses, including incorporated parent and subsidiary firms.

The net effect is that these numbers for new business formations are significantly lower than those used in previous editions of *The State of Small Business.* However, they probably offer the most accurate perspective of actual start-ups, given that there is no definitive measure. At the very least, they give a sound indication of trends in the businesses that offer the most hope for growth — those that hire people to work for them. They have therefore been used in Chart 2.2, which shows the number of actual start-ups and disappearances of businesses over the same period as Chart 2.1.

The trends shown in Chart 2.2 are similar to those shown by Chart 2.1. However, there was a lag of three or four years before the start-up activity following the recession translated into a surge of new business formations. Start-ups dipped sharply during the recession, naturally enough, recovered strongly in the following year and held steady during the year after that. Since then, however, start-ups have grown powerfully every year, as Chart 2.2 shows. The net effect has been to raise the total number of businesses in Ontario by 41% from 215,523 in 1978 to 304,418 in 1987, which is equivalent to an annual increase of 3.9%

Chart 2.2[3]
Business Starts and Stops

Number of new firms and discontinued operations, Ontario, 1978-87



The trends for discontinued firms follow the lead of start-ups, with a predictable lag, this time of about one year. Because there is such a high rate of discontinuance in the first year of business for start-ups, any increase in new business formations quickly translates into an increase in failures.

Similar problems exist for the tabulation of discontinued businesses as for start-ups. Some of the businesses counted as discontinued in the database used in this chapter have been taken over by other businesses or been transferred to another database. The data have been adjusted as far as possible to compensate for the vagaries of data collection from statistics

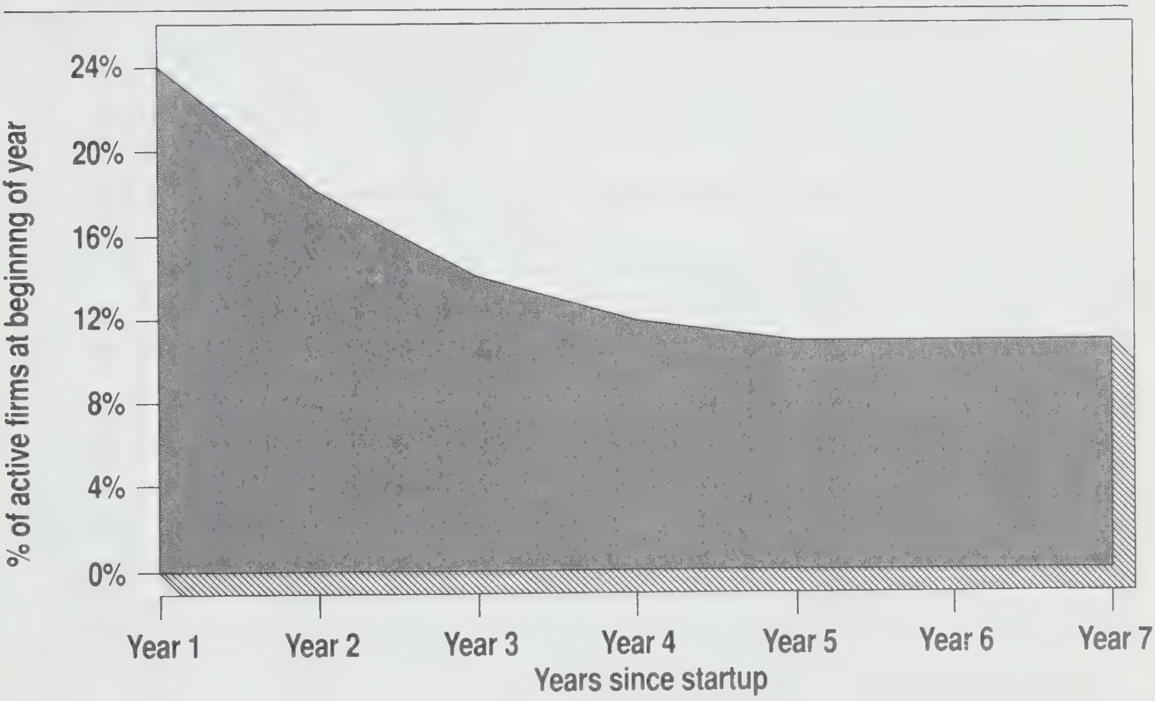
[3] Statistics Canada, Small Business and Special Surveys, in a special run for the Ministry of Industry, Trade & Technology, extracting longitudinal data on discontinued firms, by number of years since start-up, 1989

assembled for other purposes, but it is still likely there are overstatements. Again, however, the trends they exhibit are accurate and the relationship to start-ups is consistent.

These statistics show that the average life of a business is about seven and a quarter years. Almost a quarter of new firms are discontinued within their first year of operation, some because they have failed, others because they are sold or wound up. The rate at which new businesses disappear comes down sharply in the following few years, however, as Chart 2.3 shows. After about four years, the failure rate flattens out. It appears that, out of every 100 firms more than four years old at the beginning of any year, about 10 cease operations within that year.

Chart 2.3[4]
The Annual Disappearance Rate of New Businesses

Percentage of firms that fail, cease operations or are taken over, expressed as a percentage of the number of firms at the beginning of each year, Ontario, 1978-87



[4] Ibid. Statistics Canada, Small Business and Special Surveys

The effect of the rate at which businesses are discontinued is shown in Table 2.1. Only about a quarter of new firms are still operating ten years after they started. Almost half of all start-ups disappear within three years.

Table 2.1[5]
The Casualty List for Start-ups

Percentage of original firms that cease operations each year and the cumulative loss of businesses by the number of years since start-up - average for Ontario firms started during 1978-87

Years since start-up	Disappearance rate per annum %	Cumulative disappearances %
1	24	24
2	14	38
3	9	47
4	7	54
5	5	59
6	5	64
7	4	68
8	3	71
9	3	74
10	2	76

This high rate of attrition in the early years after a new business is formed is the main reason that the number of discontinued businesses rises so sharply in Chart 2.2 after 1983.

Of course, many of the people whose businesses fail come back and try again. The fate of owners should not be confused with that of their early businesses. The demographic profile[6] of the owners of these new ventures is as follows:

- More than 80% of them were born in Canada and 95% are Canadian citizens;
- Almost 30% are women;

[5] Ibid. Statistics Canada, Small Business and Special Surveys
[6] Ibid. *Study of Business Start-ups in Canada.*

- Two-thirds have more than a high school education (44% completed degrees at university or community college and 23% studied there but didn't graduate); and
- Their average age was 38 and 70% of them were aged 25 to 45. Only 7% were younger than 25.

Preparation and Expectations at Start-up

Not everyone who starts a business expects it to grow into a megacorporation. A recent study[7] conducted for the Ministry of Industry, Trade & Technology found that about half of new businesses expect to grow big and 40% expect just to make a living. By the time these people responded to this study's survey in 1988, however, their expectations had become slightly more ambitious. Only 31% of the respondents expected employment in their businesses to decline or stagnate and 61% expected continued growth. Nonetheless, expectations at start-up have a significant effect on the subsequent growth of these businesses, as Table 2.2 shows. Close to one half of the people who expected just to make a living were still expecting no growth or a decline in employment in 1988, compared to less than a quarter for the ones who expected to grow big when they started.

Table 2.2[8]
Expectations Then and Now

People's expectations of growth at start-up compared to those at the time the survey was completed in 1988

Expectations of growth at start-up	Expectations of growth in 1988*: None %	Slow %	Fast %	Total %
Will grow big	23	61	16	100
Will just make a living	43	47	10	100

* Expectations were for growth in the number of employees. Those included under "None" expected either a decline in employment or no change.

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[7] *Newly formed Small Businesses in Ontario, 1982-87*, by Laventhol & Horwath, for the Ministry of Industry, Trade & Technology, 1988

[8] Ibid. *Newly-formed Small Businesses in Ontario, 1982-87*

Optimism was strongest among firms that had annual sales of more than $2 million — almost three-quarters of them expected continuing growth.

Expectations become a self-fulfilling prophecy partly because the ones who expect to grow take more trouble to prepare themselves adequately for the task. The people with the best prospects for growth at the time the survey was conducted include a disproportionate share of those who prepared business and marketing plans at start-up. More than half the entrepreneurs expecting fast growth in 1988 had a business plan at start-up and 41% had a marketing plan. Only a third of the people expecting a declining or stagnant employment prepared business plans at start-up and less than a quarter prepared marketing plans.

Even the people who started out unambitious came to appreciate the value of formal planning, however. For the sample as a whole, exactly half now have a business plan, compared to 39% at start-up; 42% have a marketing plan, compared to 27% at start-up.

One thing that did not appear to be regarded as essential was previous experience in a comparable job. Almost a third of the start-up entrepreneurs in the federal study[9] had no previous experience in the field in which they were starting their new venture. And of the ones who did have some relevant experience, only two-thirds could claim experience that was specifically related to their new venture. That means one-half of the people starting new ventures had no previous experience or only general experience in their new field.

This degree of inexperience is significantly greater than it was in an earlier study of start-ups in Ontario[10], which found that only 15% had no previous experience. Furthermore, 60% had had previous experience in running a business. It appears that start-ups after 1984 may be less conservative than their predecessors in picking their new line of business. Two-thirds of the people in the earlier study were starting their first ever new business, compared to 58% in the later

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[9] Ibid. *Study of Business Start-ups in Canada*

[10] *Newly-formed Small Businesses in Ontario, 1982-84,* by The Creative Research Group, for the Ministry of Industry, Trade & Technology, 1985

study. In both studies, however, about a quarter of the respondents had more than one active business at the time of the survey.

The one element of preparation that seemed to be consistent for all levels of expectations for future growth was the degree to which entrepreneurs seek out a financial institution to discuss financing. At start-up, 56% talked to a financial institution about financing. However, only 46% obtained a loan and a mere 22% obtained equity financing. Only 13% of unincorporated businesses obtained equity financing, compared to 27% for incorporated ones.

Corporate Status

Several studies have concluded that about one-third of new businesses are incorporated and two-thirds unincorporated. This relationship can vary, however, depending on the start-up rate. About a third of the unincorporated start-ups soon begin to turn enough of a profit that they have to incorporate within three years[11] of their start-up, so a surge of start-ups quickly leads to a higher proportion of new incorporations, many of which are no longer start-ups. Many of the remaining unincorporated firms never change status. Often their businesses are vehicles for "life-style" entrepreneurs who want to work on their own and don't intend to build a big business. Partnerships are all unincorporated, of course, and they can become quite large businesses. In general, however, the corporate status chosen by the owners has a major effect on what happens subsequently to a business.

Table 2.3 shows that the incorporated firms are more ambitious, invest more, plan more, investigate their business start-up more, have more experience, and are more meticulous in their paperwork. Inevitably, their results are better. Their sales are higher, they have more employees and they expect more growth.

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[11] Ibid. *Newly-formed Small Businesses in Ontario, 1982-84*

Table 2.3[12]
The Psychology of Incorporation

Comparison of the status and attitudes of incorporated and unincorporated businesses, at start-up and in 1988, Ontario

Status or attitude	Incorporated	Unincorporated
At start-up		
Average total investment	$116,000	$69,000
Average personal investment	$34,100	$24,500
	%	%
Personal/total investment	29	36
Percent investing less than $25,000	55	73
Talked to financial institutions	63	43
Obtained a loan	50	37
Obtained equity financing	27	13
Developed a financial statement	93	73
Had a formal business plan	42	32
Had a formal marketing plan	31	19
Expected to become a big firm	59	36
Worked out of home	25	37
Aged less than 40	48	61
Had relevant previous experience	37	22
At time of survey		
Average sales	$870,000	$360,000
	%	%
Expecting to hire more people	66	47
Prepared to borrow to expand	65	46
Percent with fewer than 5 employees	36	65

Generally, people who incorporate their new businesses are more likely to stay the course than those who do not incorporate. The federal study of start-ups[13] found that incorporated businesses accounted for 34% of all the firms in the study, but only 17% of those no longer operating in 1988 and 17% of those not yet operating. Sole proprietorships, by contrast, accounted for 44% of the firms in the study, but 63%

[12] Ibid. *Newly-formed Small Businesses in Ontario, 1982-87*
[13] Ibid. *Study of Business Start-ups in Canada*

of the firms not yet operating and 56% of those no longer operating. The balance of the firms (18%) were partnerships.

Home-based Business: Room to Grow?

People starting retail stores or manufacturing concerns have little choice but to rent or buy space for their new businesses. But in the service industries, which attract more new businesses than any other sector, it is a viable option to start the business in a garage or a room in the owner's home. It is also now quite common for people to start businesses on a part-time basis in the hope they will be able to build them up to the point where they can quit their jobs and run them full-time. These people usually run their businesses out of their homes, too.

According to the federal study of start-ups, 42% of the businesses that were registered or incorporated in 1987 were operated on a part-time basis by the owner. These people accounted, not surprisingly, for the lion's share (85%) of businesses that were not yet operating in the fall of 1988. Nonetheless, three-quarters of them were operating, so it is a popular way of starting a genuine business.

The federal study found that almost half of the start-ups in Canada are run from the home, while 40% rent their space and 10% buy it. The study on 1982-87 new businesses in Ontario, by contrast, found that only 29% worked out of their homes in Ontario at start-up, but this is certainly an under-statement because this study had a disproportionately heavy weighting of larger and incorporated firms. The incorporated firms were less likely to be started in the owners' homes (25% compared to 37% of unincorporated firms), as were larger firms (13% of firms with more than 20 employees started in the home, compared to 38% of firms with fewer than five employees)[14].

The Ontario study nonetheless illustrates some important trends. Many of the firms that are started in basements and garages grow enough to move into rented space. By the time the survey was conducted in 1988, two-thirds of the

[14]The statistics quoted from the study on newly formed businesses in Ontario between 1982 and 1987 are adjusted to remove non-respondents.

businesses were renting space, compared to a half at start-up. This development took place principally in unincorporated firms, 38% of which rented space at start-up, but 57% of which were using rented space when the survey was conducted.

Investment at Start-up

The average investment in new firms registered or incorporated in 1987 was $58,300, according to the federal study of start-ups[15]. This is more than double the average investment of newly-formed firms in Ontario in 1982-84[16], which invested an average of $24,000. It is likely that the Ontario study is closer to the average for all start-ups, because the federal study is under-represented in service industries, which require much smaller investments at start-up. Only 39% of the firms in the federal study were in the service industries, compared to 56% in the Ontario study. (Two-thirds of the increase in business owners between 1981-86 were in services — see chapter 3). The average investment of firms in the 1982-87 study of new businesses in Ontario is much more again, at $103,000, but this reflects that study's heavy weighting of bigger firms and incorporated start-ups, both of which have significantly higher investments.

The average investment in start-ups can vary enormously, depending on the weighting a study gives to firms that start with a bang. In a previous study of 84 fast-growth firms[17], the average investment at start-up was $2.4 million. Even if the largest 18 of those firms are excluded, the average investment of the rest was still $350,000. The firms that start with a bang invest large sums of money that distort the averages if they are not given accurate weightings. In the federal study, for example, 82% of the firms invested less than $75,000, averaging $17,200, but their total investment accounted for only 24% of the total for all firms. As Chart 2.4 shows, 2% of this study's firms, which invested more than $500,000 each, accounted for 26% of the total investment.

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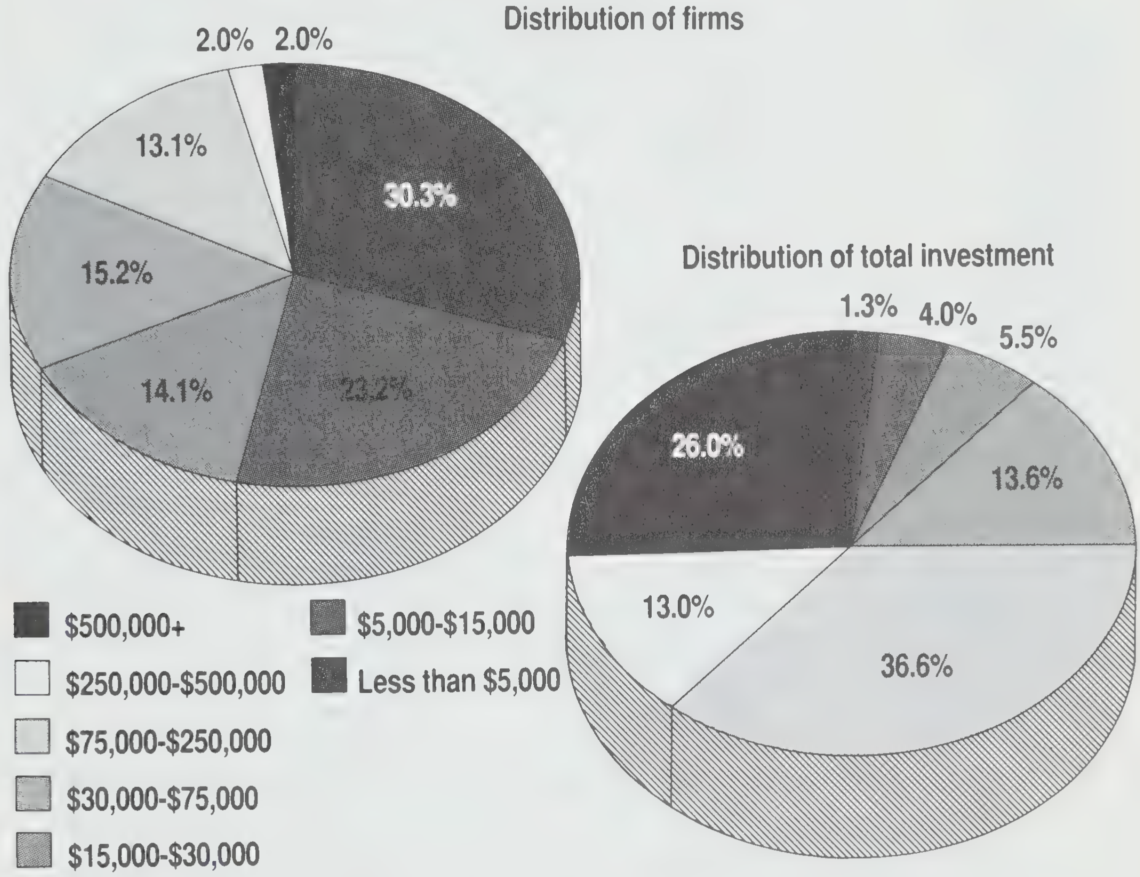
[15] Ibid. *Study of Business Start-ups in Canada*

[16] Ibid. *Newly formed Small Businesses in Ontario, 1982-84*

[17] *Ontario's Successful Businesses*, by Decision Marketing Research Limited, 1987. See The State of Small Business, 1987

Chart 2.4[18]
Start-up Investment

Percentage distribution, by size of start-up investment, of the number of new firms and of their total investment



The funds for these investments come from a wide variety of sources. Several recent studies have shown that the relative importance of the sources is fairly consistent, although the overall level of funding varies from study to study. As Table 2.4 shows, the main difference lies in the fast-growth firms, which invested an average of $2.4 million at start-up and therefore needed to raise a lot of money from financial institutions, other investors and related companies. In the federal study, the start-ups used an average of 1.7 sources of financing, apart from their own funds.

[18]Ibid. *Study of Business Start-ups in Canada*

Table 2.4
Sources of Funds for Start-ups

Percentage of firms in each of four recent studies that used funds from the sources shown

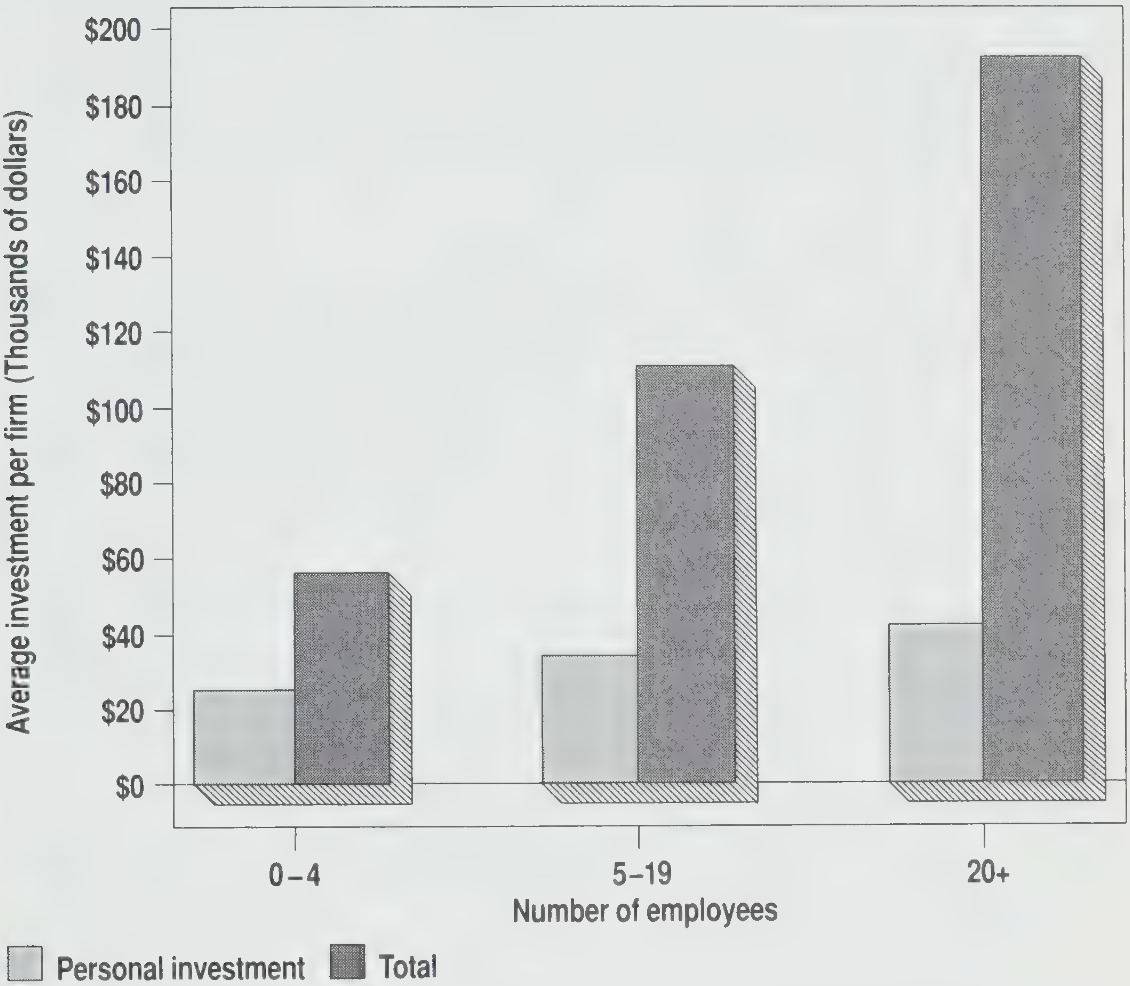
	Start-up firms in four different studies, showing percentage that used each source of funds			
Source of funds	Federal start-ups Canada 1987	New Businesses in Ontario 1982-87	Fast-growth Ontario 1974-84	Cross-section Ontario 1982-84
	%	%	%	%
Personal	82	n/a	54	100
Banks/Financial institutions	35	36	66	27
Family	18	9	17	14
Other investors	7	15	25	16
Related companies	7	n/a	14	-
Friends	5	5	6	8
Government	5	n/a	3	-

Note: The four studies are, in order, Study of Business Start-ups in Canada, Newly-formed Small Businesses in Ontario, 1982-87, Ontario's Successful Businesses and Newly-formed Small Businesses in Ontario, 1982-84.

The study on new businesses in Ontario during 1982-87 analyzed the personal investments made in different sizes of firms. The variation in the dollar investment by the owners varies surprisingly, so the percentage of the investment funded by personal financial resources declines with the size of the firm, as Chart 2.5 shows. The personal funds of the owners of the bigger firms accounted for 22% of the total investment, compared to 43% for the smallest.

It would appear that people who expect their companies to grow rapidly rely less on their own financial resources. The owners who expect their firms to decline or remain stable provided 43% of their initial investment from their own resources, while those who expect to grow provided only 28%.

Chart 2.5
Whose Money Was on the Line



Entrepreneurs are also careful about retaining control over the equity in their firms. Three-quarters of the people in the study of new businesses during 1982-87 expected to maintain or increase their ownership of their firms. If they were to decide to expand, almost 60% of them would be prepared to borrow money to do it. The ones expecting to grow were more prepared to borrow (69%) than those who did not expect to grow (51%).

If they were given an extra $100,000 to invest, the most popular choice of entrepreneurs in the 1982-87 new businesses study would be to buy or lease more equipment, followed by renting or buying more space. The next three most popular choices were, equally, to hire more staff, train them and to pay down loans. The ones who expected to grow fast went first for more space, second for hiring more people and third for more training. The need for more equipment is concentrated in the smaller and unincorporated companies.

The Motivations of Entrepreneurs

There have been countless studies on the motivations of entrepreneurs over the years and, although there are some elements of a consensus, it is still a controversial subject. Albert Shapero found in the U.S.[19] that people who start businesses are often corporate refugees. Russell Knight confirmed the phenomenon in Canada[20], with an interesting expansion on the nature of the refugees. These refugees are involuntarily pushed out of previously comfortable niches and forced to swim on their own, just as much as they are impelled by positive forces inside themselves. David McClelland[21] found that entrepreneurs are motivated principally by the need to achieve. Many others have observed, among other motivations, the desire of new entrepreneurs to be their own boss, to make good money and to enjoy the challenge of pitting themselves against more powerful opponents.

Recent studies in Ontario and Canada have shown that the major entrepreneurial motivations have been consistent in the recent past. There have, however, been some minor shifts in emphasis, as Table 2.5 shows, the most notable being the increasing desire to make money.

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[19] *The Displaced, Uncomfortable Entrepreneur*, by Albert Shapero, *Psychology Today*, 1975

[20] *Entrepreneurship in Canada*, by Russell Knight, *Journal of Small Business in Canada*, 1983

[21] *The Achieving Society*, by David McClelland, D. van Nostrand, 1961

Table 2.5
Why People Start Businesses

Motivations of people who start their own firms, according to four recent studies in Ontario and Canada

	Rankings within motivation studies**			
Motivation	**Federal start-ups Canada 1987**	**New businesses in Ontario 1982-87**	**Cross-section Ontario 1982-84**	**Fast growth Ontario 1974-84**
Sense of accomplishment	1	n/a	n/a	=6*
To make money	2	=1	2	3
To be my own boss	3	=1	1	1
To adapt my own approach to work#	4	4	4	=6
To use my skills and training#	5	5	5	2
To develop an idea or product	6	n/a	n/a	9*
Saw a need	n/a	3	3	4
To make a living	n/a	6	6	=6
Opportunity/challenge	n/a	n/a	n/a	5*
Average year of start-up	**1987**	**1984**	**1983**	**1970s**

\# "To use my skills and training" was taken as equivalent to "had previous relevant experience". Also, "To adapt my own approach to work" was taken as equivalent to "always wanted to run a business".

* Respondents mentioned these motivations without prompting. All other responses were to questions that specifically mentioned a motivation.

** The four studies are, in order, Study of Business Start-ups in Canada, 1987, Newly-formed Small Businesses in Ontario, 1982-87, Newly-formed Small Businesses in Ontario, 1982-84, and Ontario's Successful Businesses.

"To be my own boss" used to be the biggest motivator, but it has dropped to second place after "to make money" in the course of the 1980s. If "sense of accomplishment" is ignored for the moment (it was suggested only in the most recent questionnaire, so it's impossible to determine any trend with it from these studies), the consensus of these studies is that the current most popular motivations are:

1. To make money;
2. To be my own boss;
3. Saw a need for my product or service;
4. Always wanted to run a business, to do it my way;
5. Wanted to use my experience and skills; and
6. Needed to make a living, economic necessity.

The rankings are different for some of the sub-groups of the entrepreneurs interviewed for the above studies, of course. People who expect to grow in the study of new businesses in Ontario during 1982-87, for example, rank "saw a need" as the top motivation, but those who don't expect to grow mentioned "to be my own boss" twice as frequently as "saw a need".

It's not certain, either, that the top two motivators have indeed switched places. It's possible that making money has always been the top priority and suffered only a temporary relapse during the recession years. In the 1982-87 study, this motivation ranked first before 1982 and after 1984, but only third in 1982-84. This might reflect the reality that during the recession years, making much money must have seemed a rather distant prospect.

The debate about motivations extends beyond these studies, however. There are other motivations that these studies did not explore but which are important to entrepreneurs, notably the need for a sense of achievement and enjoyment. Most of the above studies have been hampered by questionnaires that offered a limited number of options to the respondents, who seldom took the initiative of suggesting other motivations important to them.

A major study conducted in 1987 explored a wider range of motivations and found quite different results from the four studies discussed above. The Canadian portion of an international study on "Why people decide to start a new business: The effect of cultural values on entrepreneurs" comes to strikingly different conclusions, as Table 2.6 shows.

The primacy of the need to achieve is clear in this study. This is an important motivation for entrepreneurs, who could not overcome the many obstacles they encounter if they did not have this strong urge to accomplish their goals. Interestingly, the need for recognition for these achievements is not as important, ranking only 21st.

The second, third and fourth motivations in the four studies discussed previously rank just as high in the cross-cultural study. "To be my own boss", "Saw a need" (or "Seized an opportunity") and "adopting my own approach" (or "do it my way") ranked second, fifth and third respectively in the 1987 study.

Table 2.6
A Cultural Study of Motivation in Canada

	Motivation	Percentage claiming this as a motivation %
1.	Sense of accomplishment	76
2.	To be my own boss	75
3.	Freedom to adapt my own approach to work	66
4.	To have variety and adventure in my work	64
5.	To seize an opportunity	64
6.	To start and grow a new business	63
7.	The opportunity to lead rather than be led	60
8.	To make a direct contribution to the company's success	59
9.	To be able to develop an idea for a product or service	58
10.	To keep learning	54
11.	To better use my training or skills	51
12.	To control my time	50
13.	It was a time in my life when it made sense	50
14.	To be able to work with people I choose	43
15.	To be innovative, in the forefront of technology	42
16.	To have fun	42
17.	Desire to have high earnings	42
18.	To have greater flexibility for myself and family	41
19.	To be able to work with people I like	37
20.	To give myself and my family security	35
21.	To achieve something and get recognition for it	34
22.	To be respected by friends	32
23.	Frustrated in previous job	26
24.	To be able to work where I and my family want	25
25.	To achieve a high position for myself in society	23
26.	Not to work for an unreasonable boss	16
27.	To contribute to the welfare of my relatives	16
28.	To have access to fringe benefits	15
29.	Needed more money to survive	15
30.	To become part of a network of entrepreneurs	14
31.	To contribute to the welfare of my community	12
32.	To increase the prestige of my family	8
33.	To follow the example of a person I admire	5
34.	To have more influence in my community	5
35.	It was the only thing I could do	5
36.	To escape unsafe working conditions	5
37.	I wanted to continue a family tradition	3
38.	To contribute to the welfare of my ethnic group	1

Beyond these three, however, the results of the 1987 study give a quite different picture. Five concepts are introduced in the 1987 study that were not in the earlier ones:

- Enjoyment is most apparent in two of the replies — "to have variety and adventure in my work" (#4) and "to have fun" (#16). It's also a big part of "being innovative, at the forefront" (#15), as this involves self-fulfillment;
- Challenge is suggested by variety and adventure (#4);
- Winning in business is the core element of "starting and growing a new business", "the opportunity to lead rather than be led" and "to be able to make a direct contribution to the company's success", which ranked 6th, 7th and 8th;
- The need to develop an idea for a product or service (#9) is a critical motivation for many, many entrepreneurs, particularly technologically oriented people; and
- Affiliation needs are inherent in "to work with the people I choose" and "to work with people I like", which ranked 14th and 19th. These are not common in entrepreneurs, but are still a motivational factor for an important minority.

Surprisingly, the need to make good money ranks only 17th, far below the first place in the four studies discussed earlier. Money is a difficult subject to interpret, however, because so many people find it as hard to deal with their own wealth as to deal with other people's attitudes toward their wealth.

In another recent study[22], entrepreneurs' attitudes toward money were found to be very complex. The conventional wisdom, consistent with the 1987 cross-cultural study, is that entrepreneurs are not driven by the need for money per se, but rather that they value it as a means of keeping score of how well they are doing. An equally more common attitude among the entrepreneurs in this study was that they unabashedly liked it because of what they could buy with it.

These entrepreneurs were all successful entrepreneurs and included people who have been in business for a wide

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[22] *The Entrepreneurial Edge,* by Donald Rumball, Key Porter, 1989

range of years, from start-ups to 45 years. The median period of ownership was 10 years and a quarter of them had owned their firms for less than five years. Their motivations therefore inevitably differ from those of people who are embarking on a start-up, but there are striking similarities, as Table 2.7 shows.

Almost a third (30%) of the entrepreneurs in this study said money was important to them and nearly as many (27%) said emphatically it wasn't. However, almost a third of those who said money was not important acknowledged that it had been important before they became successful. If these people are counted as being motivated by money, even if only at the start-up stage, then money comes very close to the top of the rankings of motivators, at 41%.

Table 2.7[23]
Motivations of Successful Entrepreneurs

	Motivation	Percentage who said this motivates them %
1.	Having fun	44
2.	Building a lasting organization	34
3.	Money	33
4.	Winning in business	29
5.	Recognition	26
6.	Sense of accomplishment	23
7.	Seeing people fulfill their potential	21
8.	The challenge	14
9.	Improving the world in some way	12
10.	Problem solving	10
11.	Producing a top-quality product	10
12.	Meeting interesting people	9
13.	Independence	8
14.	Power	8
15.	Proving a point to doubters	7
16.	Creativity	6
17.	Helping the family	4

[23]Ibid. *The Entrepreneurial Edge*

The most popular motivation for entrepreneurs in the cross-cultural study conducted in 1987 was the need for a sense of accomplishment (76%). In the study of successful entrepreneurs, several sub-themes of accomplishment were identified — building a lasting organization, winning in business, improving the world in some way in addition to a sense of accomplishment. If these motivations are pooled, then 74% of the entrepreneurs gave this as a motivation.

After a sense of accomplishment, the studies diverge sharply. Six of the next seven in the start-up study reflect the forces that dominate when entrepreneurs are starting their own businesses. Their major need at this stage in a business is an outlet to express themselves outside the constraints of being an employee. These are: the need to be their own boss (75%), which is seldom something that motivates anyone who already has a successful business; setting their own approach to work (66%); variety and adventure (64%); starting and growing a new business (63%); the opportunity to lead rather than being led (60%); and making a direct contribution to a company's success (59%). As was mentioned earlier, there is a strong element of winning in business in some of these, but it is directed at a different challenge from that perceived by entrepreneurs who have already succeeded.

Only much lower in the rankings of start-ups do motivations comparable to those of established entrepreneurs start to appear: seizing an opportunity (64%) was the highest at fifth; high earnings (42%) was 17th; achievement and recognition (34%) was 21st; and having fun (42%) was 16th.

[The total percentages of people mentioning each motivation are higher in the cross-cultural study than in *The Entrepreneurial Edge*, mainly because it was performed by sending out a long and detailed questionnaire, which prompted responses to specific questions relating to hypothetical motivations. In the study of successful entrepreneurs, the interviews were open-ended. The entrepreneurs were not asked to respond to specific hypotheses, but were asked to articulate, without prompting, what drives them. The replies of each one almost certainly do not cover all the drives that motivate that individual, but together, they appear to cover all the major motivations, in roughly the right proportions.]

Women

The percentage of start-ups run by women appears to be lower in most studies than it really is in the whole economy. The census of Canada showed that the growth in business owners between 1981 and 1986 was dominated by women, who accounted for 56% of the increase in Canada and 42% in Ontario (see next chapter). Yet, in all the studies in this chapter, women never accounted for more than 30%, and often for a great deal less.

Whatever the sociological reasons for this, it would appear that women are generally adopting a lower profile and easing into the world of entrepreneurship more cautiously than men. It's likely that many of the firms run by women will mature into more aggressive businesses in the next few years. For the moment, however, women are more likely than men to have no employees and run an unincorporated firm, often out of their homes. As Table 2.8 shows, their attitudes and ambitions are quite different.

Table 2.8[24]
Comparison of Start-ups by Men and Women

Comparison of men's and women's business statistics and attitudes

Number of employees	**Women** %	**Men** %
Less than 5 employees	53	43
More than 20 employees	11	23
Annual sales		
Less than $100,000	23	13
More than $1 million	9	27
Growth expectations		
No change	36	27
Slow growth	43	48
Fast growth	7	13

[24] Ibid. *Newly-formed Small Businesses in Ontario, 1982-87*

Why Firms Fail

In the federal study on start-ups, 5% of the firms that had registered in 1987 had failed by the fall of 1988, when the interviews were conducted. The reasons they gave for their failure are shown in Table 2.9.

Table 2.9[25]
Why New Firms Fail

The reasons given for the discontinuance of operations by firms that registered in 1987

Reason for failure	Percent responding
	%
Couldn't make enough money at it	30
Difficult to market the product	25
Problems with financial backing	22
It wasn't what I wanted	15
Took a full-time job; no time	8
Personal reasons (accident, illness, moved)	6
Production problems	6
Problems with associates, distributors	6
Problems with manpower	5
Market too small	5
Problems with government	3
Too much competition	2

These firms said they needed assistance most in obtaining more and better information (see chapter 5). Two-thirds of them cited this need. Less vital needs were grants (44%), counselling (42%), loan guarantees (33%), salary subsidies (26%) and training programmes (25%).

[25] Ibid. *Study of Business Start-ups in Canada*

Business Climate for Start-ups in Ontario

In its annual poll of Ontario residents, the government asks about people's perceptions of the climate for starting a business in Ontario, compared to other provinces. The results have consistently been overwhelmingly positive, as Table 2.10 shows. The level of preference declined slightly in 1989 after two exceptionally strong years. The preference levels were particularly high in Metro Toronto and Central Eastern Ontario.

Table 2.10[26]
The Climate for Start-ups in Ontario

Assessment of climate	1986	1987	1988	1989
	%	%	%	%
Very good	39	53	52	40
Somewhat good	44	36	36	40
Good	**83**	**89**	**88**	**80**
Somewhat poor	8	4	6	9
Very poor	2	3	2	4
Poor	10	7	8	13
No opinion	7	4	4	7

The same poll revealed a strong perception, by two-thirds of the respondents, that the policies of the government favour business rather than labour. This perception was particularly strong among the unemployed, those aged 18 to 24, those with community-college educations and members of unions.

[26] *Focus Ontario*, a poll performed for the Ontario government by Environics Research Group, 1989

CHAPTER 3
THE CHANGING PROFILE OF SELF-EMPLOYED ONTARIANS

In the first half of the 1980s, the steady flow toward self-employment raised the number of people in Ontario who are their own bosses to almost 408,000 in 1986. That's 14% more than the total of 358,000 in 1981[1], and a significantly faster growth rate than the 10% by which the number of employees in the province increased during the same period. Self-employed people accounted for 8.3% of the workforce in 1986, up from 8.0% in 1981.

Ontario is leading the rest of Canada in the increase of self-employed people. During 1981-86, the number of self-employed people in Canada grew 10% to 1,209,000, a somewhat slower growth rate than Ontario's 14%. However, Ontario is still lagging the rest of the country in the proportion of its labour force that is self-employed. By 1986, although almost 38% of the Canadian labour force was in Ontario, only 34% of the self-employed were in Ontario.

There is, however, an important distinction within the ranks of the self-employed. Generally speaking, people who incorporate their firms are more committed to their businesses and more serious about growth than those who are unincorporated. It's true that many unincorporated businesses (which include partnerships, for example) are full-fledged and active firms, but a significant proportion of them are self-employed only on a part-time basis or they are "life-style" entrepreneurs. These people are self-employed because they prefer to be their own bosses and are often not oriented toward growth as long as their earnings are adequate. They might be compared to independent craftsmen who sell their own time and expertise, but who should not be confused with entrepreneurs, who are focussed on employing people and growing their businesses.

There is an overlap between the two. It is common for new

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[1] Small Business and Special Surveys Division, Statistics Canada, based on the Census of the Population of Canada, 1981 and 1986. Unless otherwise stated, all statistics in this chapter are from this same source.

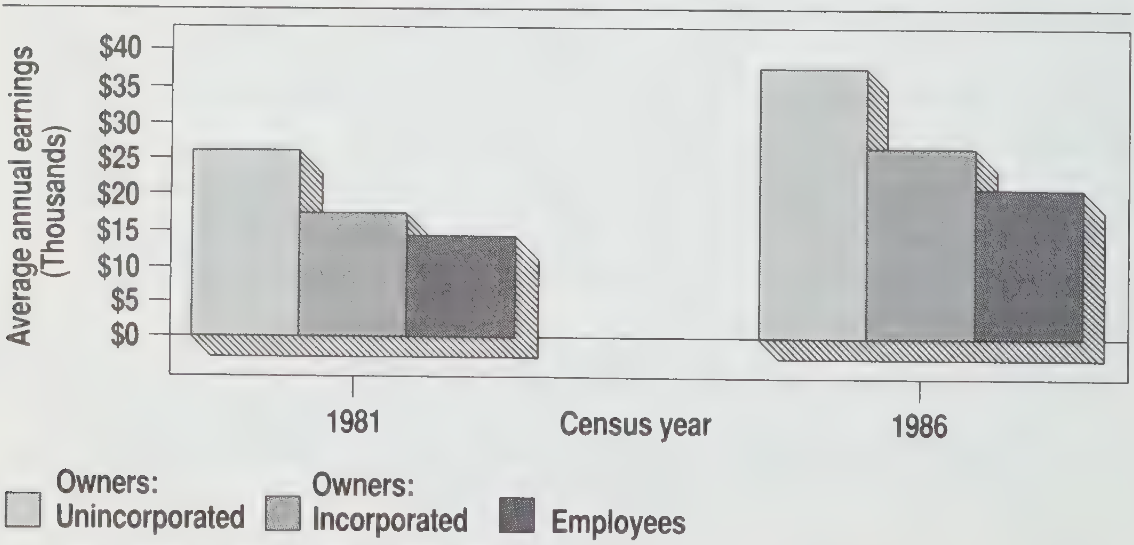
entrepreneurs to start out as unincorporated sole proprietors while they find their feet. Once they establish themselves and start earning significant profits, they usually incorporate, if only for tax reasons. Because of this and the factors mentioned earlier, the earnings generated by incorporated businesses are invariably higher, by a wide margin, than those generated by unincorporated firms.

It is therefore noteworthy — and perhaps a sign of the maturing of the trend toward entrepreneurship — that the increase in the number of owners of incorporated businesses in Ontario during 1981-86 was 27%, compared to an increase of only 9% in the number of self-employed people in unincorporated firms. The percentage of the self-employed who have incorporated their businesses rose to 32% in 1986 from 29% in 1981. This imparts greater strength and earning power to the growth in the total number of self-employed Ontarians than is implied by the 14% average growth in self-employed people.

As Chart 3.1 shows, the average reported earnings of owners of incorporated businesses are about three-quarters as much again above those of employees, while the unincorporated self-employed earn only a quarter more than employees.

Chart 3.1
It Pays to Be Self-Employed

Comparison of the average earnings of employees and the self-employed in Ontario in 1981 and 1986



The wage gap between employees and self-employed people as a whole increased during 1981-86, when the average earnings of the self-employed grew by 47%, compared to 43% for employees. This raised their average earnings to $30,496 in 1986, or 43% more than the average for all employees of $21,317.

However, the gap in earnings between the two classes of self-employed people is shrinking. Owners who incorporated their firms increased their earnings by 41% between 1981 and 1986, compared to 48% by the unincorporated self-employed. The earnings that owners drew from incorporated firms exceeded the earnings of the unincorporated self-employed by 38% in 1986, compared to 45% in 1981.

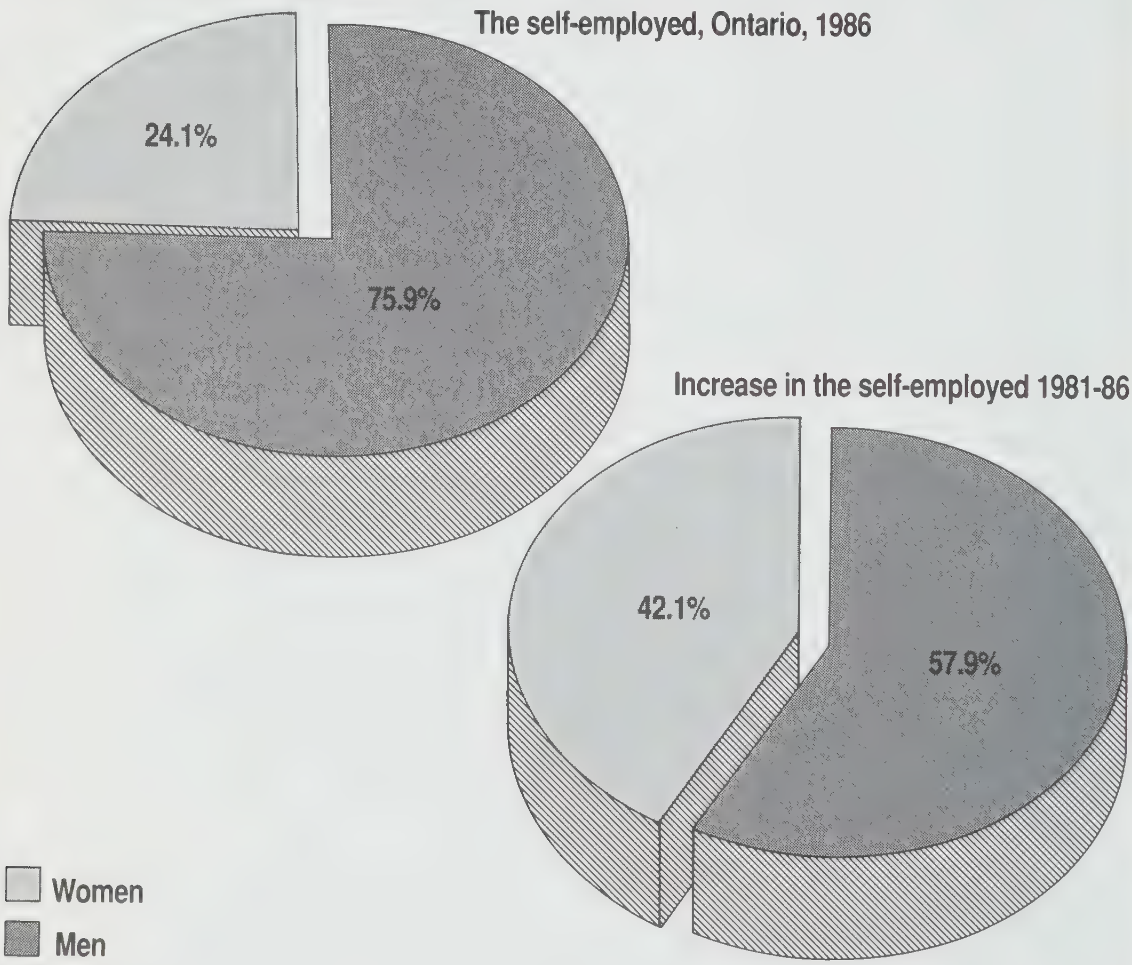
Women

Women have played a vital part in boosting the ranks of the self-employed, as is shown by Chart 3.2. During the period 1981-86, women accounted for 42% of the increase in the number of self-employed Ontarians. This is somewhat lower than the figure for all of Canada, where women accounted for 49% of the increase in self-employment, but this reflects a catch-up by women in other provinces rather than slow growth in Ontario. In 1981, 19% of the self-employed in Canada were women, compared to 22% in Ontario. By 1986, women accounted for 24% of the self-employed in Ontario and 22% in Canada.

This has led, naturally enough, to the widespread assumption that women are leading the trend toward entrepreneurship, but this is not so — at least, not yet. Men and women are both turning to self-employment at close to their historical rates, which were 4.10% of the workforce for women and 10.85% for men in 1981. The major reason for the rapid increase in women business owners is that women are entering the workforce in far greater numbers, accounting for two-thirds of the growth during 1981-86. For both men and women, the growth rate of the self-employed during 1981-86 was about two and a half times the growth rate of the workforce as a whole. The result was that the proportion of the workforce that is self-employed rose by an almost identical amount during the period to 4.53% for women and 11.25% for men.

Chart 3.2
The Growing Role of Women

Women's share of self-employed Ontarians in 1986 and their corresponding share of the net gain in self-employment during 1981-86

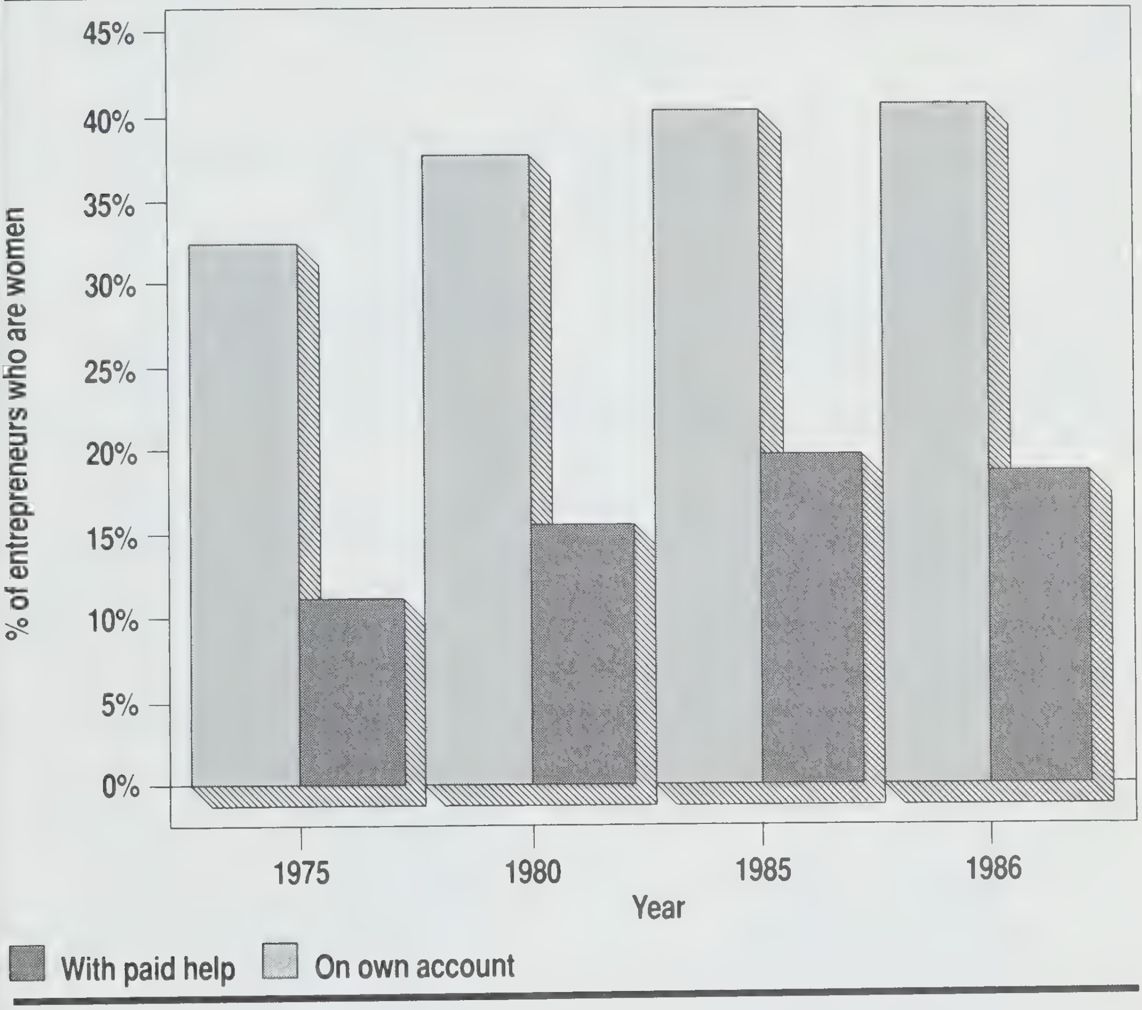


Moreover, the growth of women entrepreneurs is still weighted toward those who work for their own account only, without employing anyone else. As Chart 3.3 shows, although women represent almost a quarter of all entrepreneurs, they represent less than a fifth of those who employ other people. By contrast, about 40% of the entrepreneurs who work for their own account are women. In the 11 years to 1986, their share grew in both categories, however, with the faster proportional growth among those with paid help.

Chart 3.3[2]

The Increase in Women Entrepreneurs

The percentage of all entrepreneurs in Ontario who are women, for those who operate on their own account and for those who employ people.



The preponderance of women in the net growth of the workforce resulted in a 27% growth in the number of self-employed women during 1981-86, as Table 3.1 shows. This is considerably faster than the 10% growth rate recorded by men. In Canada as a whole, self-employed women increased at the same rate, 27%, while self-employed men increased somewhat slower, at 6.5%.

[2]Enterprising Canadians: The self-employed in Canada, October, 1988. Labour and Household Surveys and Analysis Division, Statistics Canada

Table 3.1
Growth in Self-Employment Among Men and Women

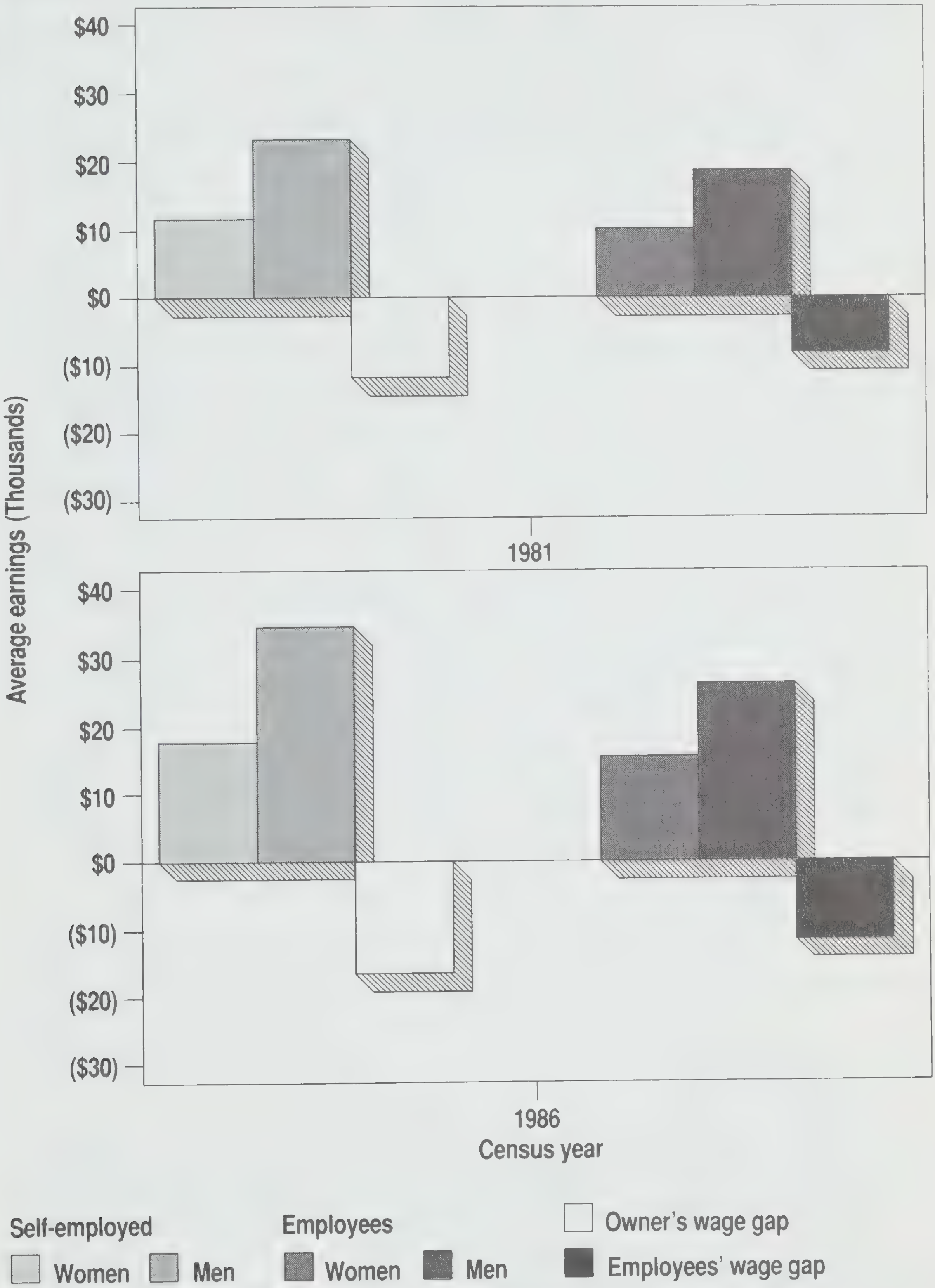
Growth rates in Ontario for self-employed, employees and total labour force, by gender, 1981-86

Employment Status	Number 1981	Number 1986	Growth rate 1981-86
WOMEN			%
Self-employed	77,075	98,190	27.4
Employees	1,801,225	2,071,600	15.0
Total	1,878,300	2,169,785	15.5
MEN			
Self-employed	280,585	309,605	10.3
Employees	2,305,160	2,442,845	6.0
Total	2,585,745	2,752,455	6.4

The wage gap between men's and women's earnings is actually bigger for the self-employed than it is for employees, as Chart 3.4 shows. The earnings of self-employed women were 51.5% of those of self-employed men in 1986, which is an improvement over 1981, when their earnings were only 49.1% of those of men. However, employees made even better progress. Women employees' earnings as a percentage of men's rose 3.5 percentage points during the same period to 57.7% in 1986. This was not because self-employed women failed to make adequate strides, however. On the contrary, self-employed women increased their earnings by 56% during the period 1981-86, a better performance than female employees who increased their earnings by 51%, and a better performance than all the men. However, self-employed men enjoyed much stronger earnings growth than men employees (49% compared to 42%), so the wage gap shrank less among the self-employed than among the employed.

Chart 3.4
The Wage Gap

The wage gap between men and women for self-employed people and employees, Ontario, 1981 and 1986



The critical difference between self-employed men and women is that women have a far larger proportion of unincorporated businesses than men. In 1986, almost three-quarters of the women-owned businesses were unincorporated, compared to two-thirds of the men's. Since unincorporated firms generate much lower earnings for their owners than incorporated firms, this has meant self-employed women don't benefit from self-employment as much as men. On average, self-employed women earned 17% more than female employees in 1986, which pales in comparison with self-employed men, who earned 31% more than male employees.

As Table 3.2 shows, unincorporated businesses delivered dismal earnings to their women owners compared to men owners. This is probably because of the way women grow their businesses. Chapter 2 showed that women are more likely than men to start businesses from their homes, frequently on a part-time basis, and to build their businesses more cautiously. Once their earnings start rising, they expand and hire employees just like men, but their gestation is longer. More than a third of self-employed women employ no-one apart from the principal[3]. Because the businesses owned by women are much younger than those owned by men, they have a higher proportion than men of fledgling businesses with low earnings. The earnings from unincorporated firms owned by women were only 63% of those from incorporated businesses. The comparable proportion for men was 77%. As a result, women with unincorporated businesses earned less than half (49%) as much as their male counterparts in 1986. For incorporated businesses, the comparable figure was 60%.

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[3] Canadian Advisory Council on the Status of Women, Background paper. Women Entrepreneurs; *Building a Stronger Canadian Economy*. Dina Lavoie, 1988

Table 3.2
Earnings from Self-Employment for Men and Women

Earnings in Ontario by employment status for men and women in 1981 and 1986 and the increase during the period

Employment Status	Average earnings 1981	1986	Increase 1981-86 %
WOMEN			
Incorporated	$16,175	$24,290	50
Unincorporated	9,856	15,315	55
All self-employed	11,394	17,765	56
Employees	10,087	15,237	51
Total	10,142	15,354	51
MEN			
Incorporated	28,781	40,810	42
Unincorporated	20,785	31,284	51
All self-employed	23,186	34,497	49
Employees	18,598	26,389	42
Total	19,103	27,313	43

Education

The self-employed are slightly better educated than employees. In 1986, 56% of them had some post-secondary education, compared to 52% of employees. Both had an almost identical proportion of people who did not complete secondary school. Education levels are, as might be expected, improving rapidly. As Table 3.3 shows, the net influx into self-employment has a significantly better education than the average for all self-employed Ontarians.

Table 3.3
The Improving Education of the Self-Employed

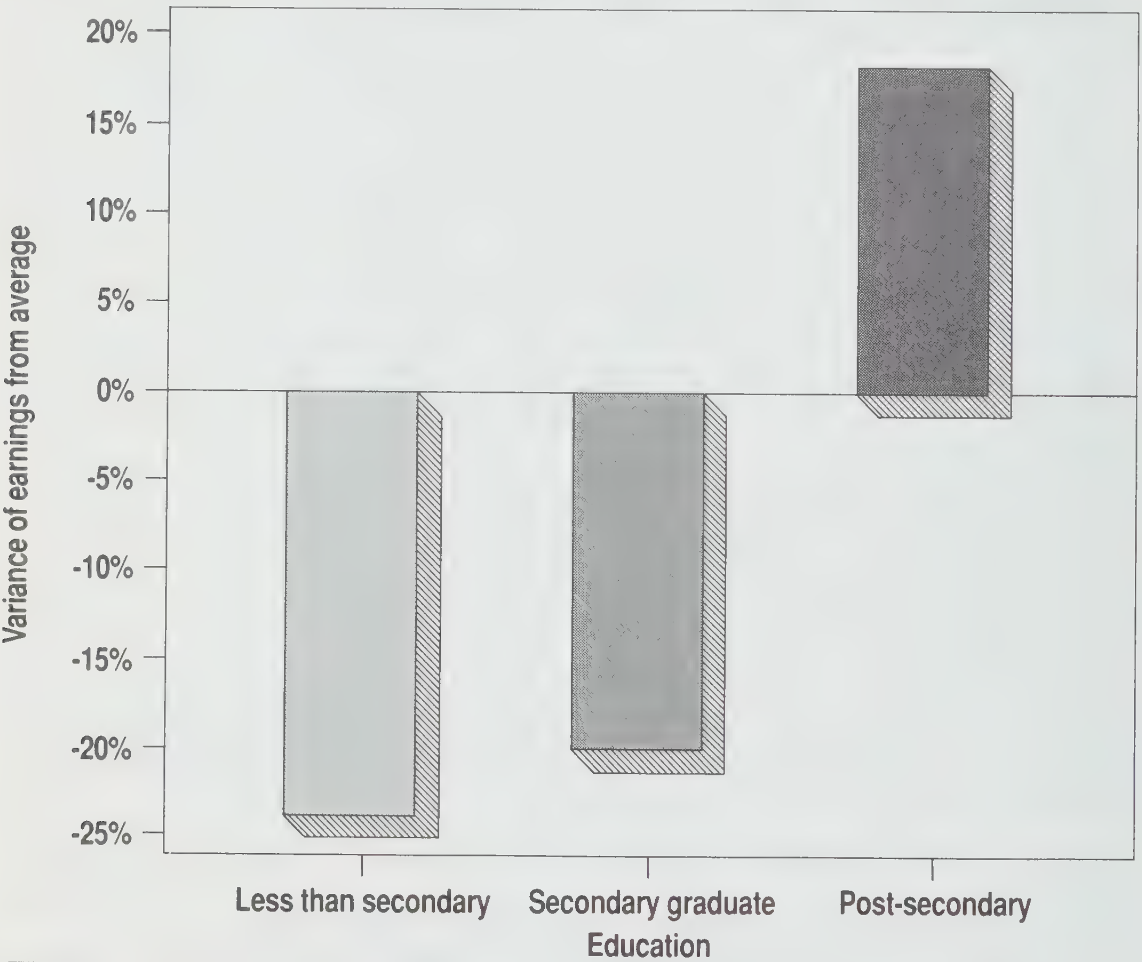
Educational qualifications of all self-employed Ontarians in 1986 and of the net increase during 1981-86

Level of education	Number 1986	Change 1981-86	% distribution of Total in 1986	Change in 1981-86
Less than secondary school	138,380	-1,580	34	-3
Secondary school diploma	40,585	+6,830	10	14
Post secondary school	228,830	+44,875	56	89
Total	407,795	+50,130	100	100

The significance of educational levels lies in their corresponding income levels. As Chart 3.5 shows, business owners with a post-secondary education earn considerably more than those with lesser education.

Chart 3.5
The Power of Education

Self-employed earnings by level of education, expressed as a percentage of the average for all levels of education, Ontario, 1986



An important element in this is the variability of earnings depending on corporate status. The range between the earnings of people with the lowest and highest education levels is 42 percentage points (-24% to +18%) in Chart 3.5, which deals with all self-employed people. This breaks down into a range for unincorporated businesses of 56 percentage points, while that for incorporated firms is 21. Once a

business is incorporated, education seems to matter less, and, presumably, business skills matter more. Since unincorporated businesses are most often partnerships or sole proprietorships, where the owners are essentially selling their personal skills, this is not surprising.

Self-employed women are in general better educated than their male counterparts: 58% had some post-secondary education in 1986, compared to 55% of the men. Equally important, only 29% of the women did not graduate from secondary school, compared to 35% of the male owners. This is changing as more women who did not graduate from secondary school start their own businesses. Almost 9% of the new female business owners during 1981-86 did not have a secondary school certificate, while the number of self-employed men with comparable education actually decreased by 12% over the same period. The men have not caught up with the women yet, however.

Self-employed women are also better educated than women employees, although the employees are gaining ground. During 1981-86, only 1% of the increase in female employees did not have a secondary school certificate, compared to 9% for those choosing self-employment. Also, 86% of new employees had some post-secondary school education, compared to 79% of the women who became self-employed.

The impact of higher education on earnings is quite different for men and women. Compared to the earnings of employees, self-employed men benefit significantly from higher education, while self-employed women benefit more if they have little education. Self-employed women with less than secondary education earn 24% more than women employees with the same education, while those with a secondary school certificate or better earn only 11% more than employees. Self-employed men, on the other hand, earn 36% more than employees if they have some post-secondary education, while those with less than a secondary school diploma earn only 18% more than employees with the same education.

This causes the wage gap for women to be more severe if they are better educated. Self-employed women with less than secondary education earn almost 60% as much as their

male counterparts, while those with some post-secondary education earn only 48% of what men with the same education earn.

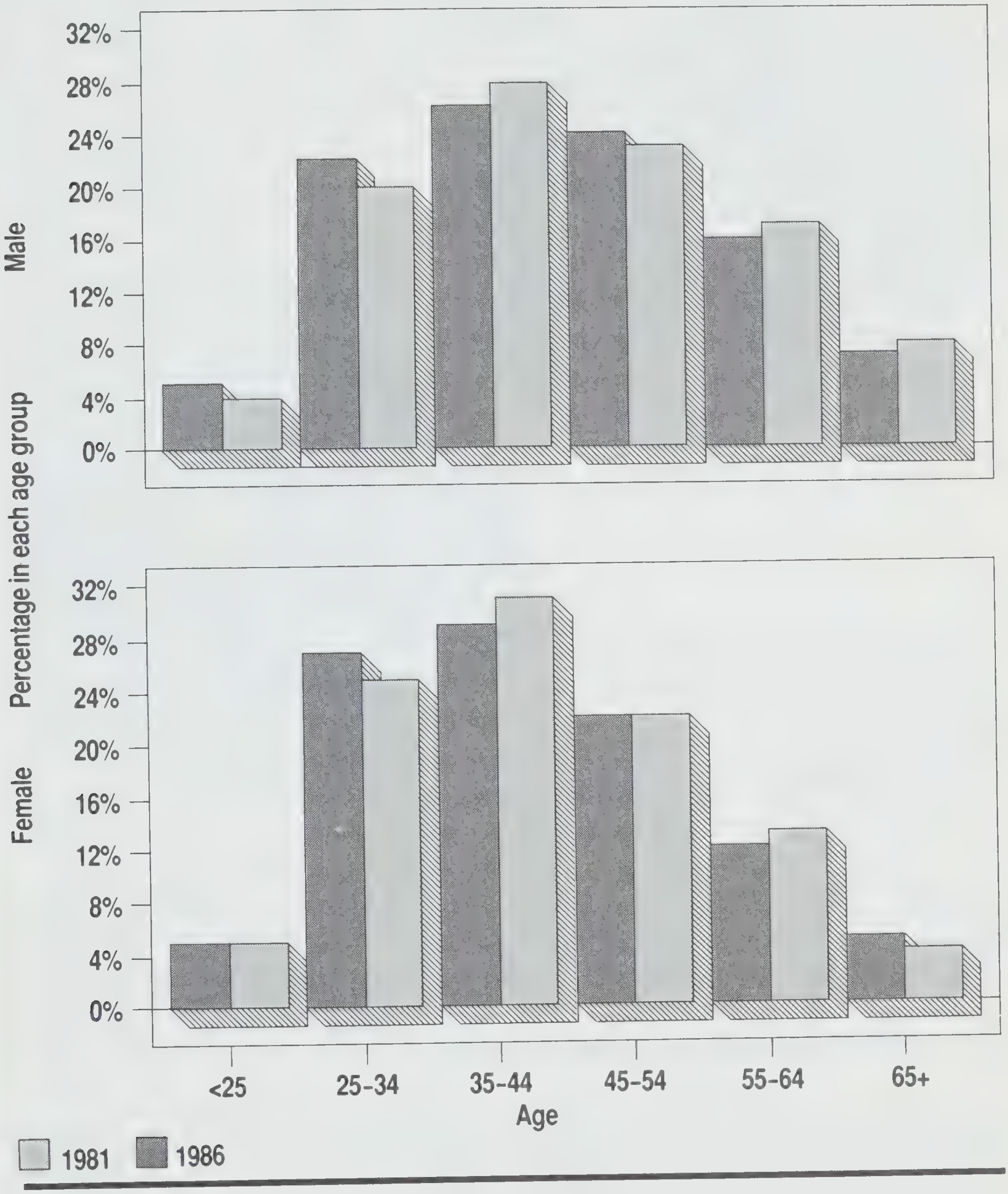
Youth

The average age of the workforce in Ontario barely changed between 1981 and 1986. The self-employed, however, were significantly older in 1986, at 44, than all other workers, at 36. As Chart 3.6 shows, the main reason for this difference is the paucity of people aged less than 25 who own their own businesses — about 4%, compared to 23% of employees who are aged less than 25. During 1981 to 1986, the percentage of men aged 45 and over increased one percentage point to 48%, while the percentage of women of that age remained constant at 39% of all women entrepreneurs. The bigger (although still small) changes were among those aged 25 to 44, where both genders decreased their percentage aged 25-34 by two percentage points and increased their share aged 35 to 44 by the same margin.

Women business owners are about two and a half years younger than their male counterparts (42.2 compared to 44.6 in 1986), and the age difference is changing very slowly as self-employed people become older. However, this conceals some interesting differences. The average age of the net influx of self-employed males during 1981-86, at 49.4, was more than five years older than the average age of all self-employed males in 1981. By contrast, the average age of the net influx of self-employed women during the same period, at 43.5, was about a year and a half older than the average for all self-employed females in 1981. However, the net influx rate for women was about three times that of men, so the impact of these age differences on the average for all the self-employed was about the same for both genders. The most striking evidence of the younger average age of the new self-employed women is that 21% of the net influx of woman owners during 1981-86 were younger than 35, compared to a 1% decline among male owners of the same age.

Chart 3.6
The Age Distribution of the Self-Employed

Distribution by age groups of the self-employed, Ontario, 1986

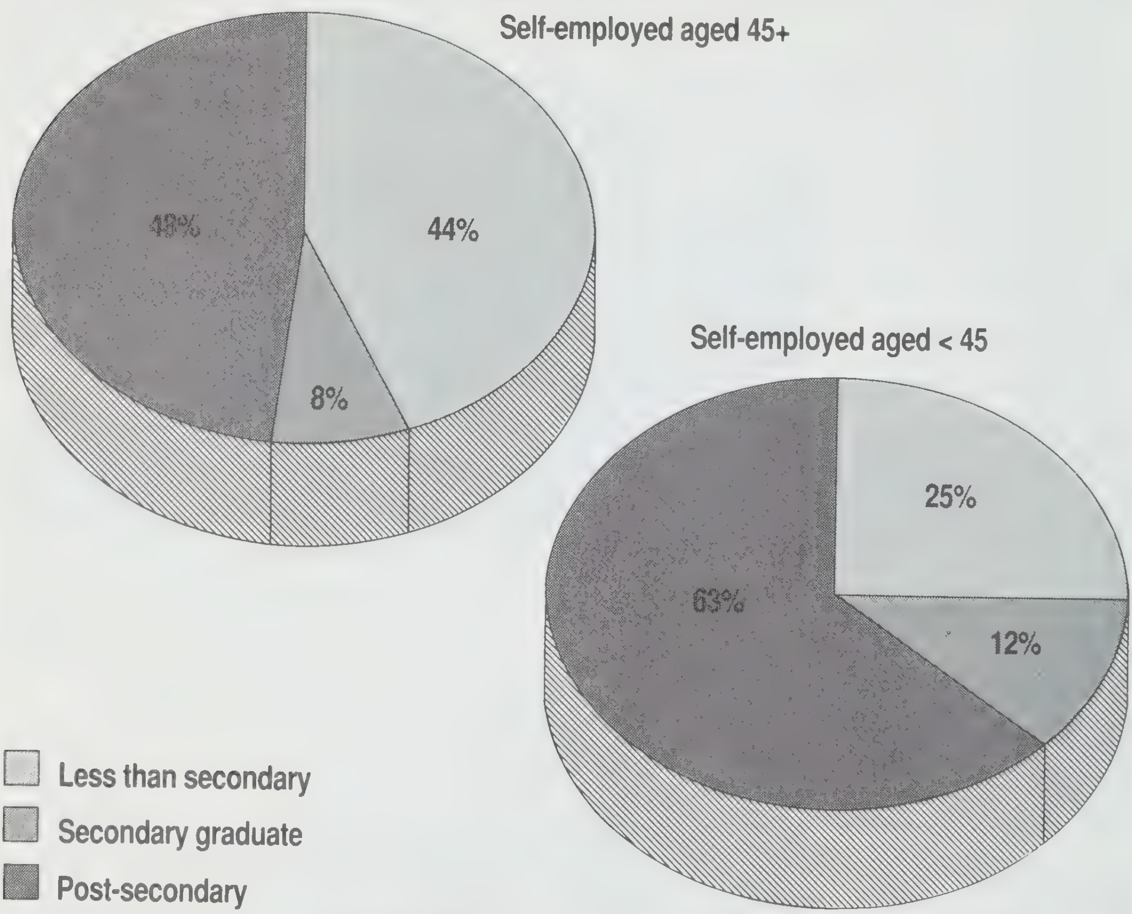


It's noteworthy that the trend is quite different among employees. The average age of the net influx of female employees was slightly higher for women than it was for men (38 compared with 35).

The young people choosing self-employment are also significantly better educated than their older predecessors, as Chart 3.7 shows.

Chart 3.7
Young Entrepreneurs are Better Educated

Educational levels of self-employed people, by age, Ontario, 1986



There is a similar tendency among employees, but it is less sharp. Among employees aged less than 45, 54% have post secondary education, compared to 44% of those aged 45 or more. The difference of 10 percentage points is much less than it is for the self-employed, as shown in Chart 3.7, where the difference is 15 percentage points.

Industry

The service industries are attracting a disproportionate share of self-employed people in Ontario and the primary industries (mainly farming) are shrinking. As Table 3.4 shows, two-thirds of the increase in the number of self-employed people during 1981-86 was in the service industries, although only slightly more than a third of all existing self-employed people were in services in 1986. The major push for this trend came

from services to business, which saw a 45% increase in business owners during 1981-86, accounting for more than half the increase in self-employed people in all the service industries.

This strong trend was particularly evident among self-employed women in service industries, who increased by 44% during 1981-86, compared with 22% for men. In services to business, they increased by 73%, compared to 38% by men. Three quarters of the increase in self-employed women during the period was in service industries, more than half of them (40%) in services to business.

This concentration on services reflects also the paucity of self-employed women in construction. A quarter of the new male entrepreneurs went into construction, compared to only five percent of the women. More than half the self-employed women in Ontario are in services and a quarter are in trade. Slightly more than half the self-employed men are in these

Table 3.4
Where the Self-Employed Like to Work

Self-employed Ontarians in 1986, the increase in self-employment within each industry, 1981-86, and the distribution of the total increase in self-employment across industries, 1981-86

Industry	Number of owners 1986	Increase, Number	1981-86 Percent	% distribution of 1986 Total	% distribution of Increase 1981-86
			%	%	%
Primary	64,180	-6,685	-9	16	-13
Manufacturing	24,195	1,465	6	6	3
Construction	55,470	8,085	17	14	16
TC&U*	17,465	2,160	14	4	4
Trade	86,130	10,005	13	21	20
FI&RE*	11,600	1,900	20	3	4
Services*	148,760	33,205	29	36	66
Other Services	50,330	12,285	32	12	25
Services to Business	49,175	15,195	45	12	30
Total	407,795	50,130	14	100	100

* Abbreviations are for Transportation, Communications and Utilities and Finance, Insurance and Real Estate. The services category includes government services. Other Services and Services to Business are included in the figures shown for Services.

two areas combined. The net influx of new business owners is accelerating this trend, with trade and services claiming 94% of the new self-employed women, compared to 81% of the men. Construction, Manufacturing and Transportation, Communications and Utilities claimed 34% of the new self-employed men during 1981-86, compared with 9% of the women.

When self-employed people choose in which industry they will start their businesses, they do not appear to be motivated by which ones offer the highest rewards. As Table 3.5 shows, the most highly rewarded business owners are in Finance, Insurance and Real Estate, yet this industry attracted only 4% of the new entrepreneurs during 1981-86. The least remunerative industry was “other services”, which is part of the service industries, and which paid its entrepreneurs 35% less than the average earnings of all entrepreneurs. Yet “other services” attracted one quarter of all the new business owners during 1981-86.

It’s more likely that trends in the industries chosen by the people who choose to become self-employed reflect the industries in which they were employees before becoming self-employed. The industries which attract self-employment seem to be those that offer the most potential for higher rewards than working for someone else. The self-employed earn 88% more than employees in the service industries and 59% more in trade. These are the two most popular industries for emerging self-employment. Finance, Insurance and Real Estate is also remunerative for the self-employed, paying double the earnings of employees — and it is no accident that the number of self-employed in this industry is growing at 20%, second only to the 29% at which services are growing.

Table 3.5
What the Self-Employed Earn in Different Industries

Average earnings in 1986 of business owners in Ontario, by industry; and how they compare with average earnings for all self-employed and the average for employees in the same industry

Industry	Average salary 1986	Self-employed earnings compared to those of all self-employed %	Self-employed earnings compared to those of employees in the same industry %
Primary	$19,476	-17	9
Manufacturing	$35,569	14	43
Construction	$25,924	-2	25
TC&U*	$27,428	23	1
Trade	$26,178	-21	59
FI&RE*	$50,848	20	99
Services*	$37,430	-3	88
Other Services	$18,713	-35	40
Services to Business	$45,891	19	106
Total	$30,496	0	43

* Abbreviations are for Transportation, Communications and Utilities and Finance, Insurance and Real Estate. The services category includes government services. Other Services and Services to Business are included in the figures shown for Services.

CHAPTER 4
THE INFORMATION NEEDS OF SMALL BUSINESS

Information is the fuel to the entrepreneurial machine. Without good information, the best strategic minds go astray, the keenest competitors misread the strengths and weaknesses of other players in the market, and even technical wizards lose their state-of-the-art technological competence. For most entrepreneurs, however, obtaining all the information they need is a pipe dream, because they simply don't have the time or the money to collect all the information they'd like to acquire. With their natural bias for action, small businesses follow the formula attributed to an executive at Cadbury's in In Search of Excellence: "Ready, Fire, Aim".

Entrepreneurs overcome this deficiency by developing an instinct for the marketplace's emerging patterns that enables them to assess correctly what information is critical and what is merely helpful. Then they acquire the minimum amount of information they need to support and guide their improvizations. This reflects their limited financial and human resources, but it also reflects their bias against the cumbersome task, so often a gigantic bore for them, of methodically accumulating meticulous facts. This approach is better suited to large bureaucracies, which invariably delay acting on their plans while they wait for more information. That's why, they are so rarely the first to innovate.

Even if entrepreneurs are usually first off the mark, however, the race doesn't always go to the first one in the market. The major corporations all catch up sooner or later, armed with marketing plans, loaded with facts, scenarios and strategies to guide their every move. Entrepreneurs have a fighting chance of surviving this inevitable onslaught only if they can maintain their grasp on the relevant information to keep one step ahead of the charging competition.

In seeking this competitive edge through their sensitivity to emerging patterns in the marketplace, entrepreneurs come equipped with a secret weapon, which they earn the hard way, through the discipline forced on every entrepreneurial

company. They have a visceral feel for their environment, because they have no choice but to stay close to their customers, employees and every facet of their business operations. It gives them an instinct few large firms can nurture in their managers.

The task of feeding that instinct with the right information is critical to the success of entrepreneurs. In general, they approach this task by establishing what information they cannot do without, and where to find it when it becomes necessary. There is an important distinction between two kinds of information needs. The kind that has received the most attention in the past several years might be called tactical information. It is necessary to implement strategies competently — how to set up financial records, how to draw up a business plan, how to do a market study, how to motivate people and many other facets of running a business. The nature of this information is easily identifiable and it is available from many sources at whatever level of sophistication and price the entrepreneur may choose.

The nature of the other kind of information cannot be identified in advance and there is no map to its source. It includes the strategies of competitors, technological innovations, the needs of potential customers, potential discontinuities in the economy or an industry, and many more variables. This might be called strategic information, since it is necessary to the formulation of strategies. Entrepreneurs who wish to succeed have to find a way of gaining access to the sources of this information, much of which they might not even know exists.

Tactical Information

Information on how to run a business has become available from a wide variety of sources in the past decade. Numerous excellent books have been published; governments and banks have developed extensive reference works for small businesses; and independent management consultants have blossomed in a market that is growing exponentially.

The critical consideration for small businesses is that they don't want to spend time accumulating all this knowledge unless they have a specific use for it. Entrepreneurs therefore generally prefer to seek tactical information in books or

manuals, because they can lay their hands on it when, and only when, they need it. As Table 4.1 shows, when entrepreneurs need assistance, printed matter is their preferred means of getting at it. Other means, such as one-on-one counselling or seminars, are less convenient because their timing cannot be controlled by the entrepreneur — and timing is critical to people under great pressure.

Table 4.1[1]
Where Entrepreneurs Like to Get Their Information

Source of assistance	Percentage who prefer this source of assistance
	%
Printed matter	51
Seminars/workshops	25
One-on-one counselling	16
Post-graduate education	5
Combination of the above	3

In a recent study of Ontario small business start-ups[2], about half the start-ups were aware of the rich supply of information from the Ontario government, but only about 10% used it. The highest level of awareness was for financing programs (57%), the lowest was for publications (47%), but the publications were most widely used (17%). The least popular government service was counselling (6%).

Strategic Information

Successful entrepreneurs draw on two main types of sources for strategic information. One is to scan all the relevant books, magazines, papers and technical material they can lay their hands on. This provides them with ideas, clues about the marketplace or straws in the wind that will help them identify information they should know exists, including business ideas. The important part of the process is identifying the need for that information; the subsequent task of acquiring that information is relatively straightforward. The

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1 *The Ohio Entrepreneurs Survey*, Catherine Ashmore, The Ohio State University, 1989

2 *Newly-formed Small Businesses in Ontario, 1982-87*, by Laventhol & Horwath, 1988

other main type of information source for entrepreneurs is a powerful network of friends and associates who can advise them and who can steer them toward opportunities or away from potential problems.

Neither of these sources of information consume much cash, but both demand a major commitment of time from entrepreneurs if they are to be effective. Many are not prepared to make that commitment, which is why their information base is shallow, unfocussed and highly intuitive. If their intuition is good (as it often is), this is not a problem, but if it isn't, they usually fail.

Entrepreneurs usually prefer to gather strategic information through personal contact, but they are also often assiduous readers. In a recent study of successful Canadian entrepreneurs[3], slightly more than half (56%) read more than an hour a day. Only one-sixth read very little and 28% read about an hour a day. Some of them are voracious readers, who may consume up to 100 periodicals a week, and it is not uncommon to find entrepreneurs who read 40 to 60 publications a week, sometimes devoting as little as an hour a day to the task.

They are also avid readers of books, often on subjects that have very little to do with their businesses. All but 6% of the people in this study said they read books regularly. Almost a third read no management or business books, preferring, in equal proportions, fiction and non-fiction on subjects other than business — notably biographies and historical fiction, from which they try to absorb the lessons of leadership from other leaders.

Personal Networks

About a quarter of the entrepreneurs in this study[4] do not make a special effort to build a personal network for business purposes. They still have circles of contacts, but they are smaller and narrower. And when they choose the members of their networks, by default or otherwise, they look for immediate, specific benefits from their acquaintance. Compared to

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[3] Unpublished material from research conducted for *The Entrepreneurial Edge*, by Donald Rumball. Key Porter, 1989

[4] Ibid

the entrepreneurs who make a special effort to build a personal network, they read a lot less (more than a quarter say they read very little).

The other three-quarters of the entrepreneurs in this study make a special effort, consciously and assiduously, to build a comprehensive network of contacts who can help them plan their business and who can contribute the fragments of information that lead to the identification of opportunities. They design their networks to include a high proportion of people who offer little immediate benefit in terms of advice or opportunity, but who may be useful to them in years to come — a sort of contingency network. Many of these people are not close to the entrepreneur, because an effective network contains its share of weak contacts who can give dispassionate views, undistorted by too close an association with the entrepreneur. Many of them maintain contacts in other industries and countries to keep their perspectives of their own businesses fresh.

For the people who make a special effort to build a network, all this takes time, of course — a commodity in short supply for entrepreneurs. This is particularly true for smaller companies that are growing rapidly. The entrepreneurs in these firms are the least likely to build networks, because they are too concerned with internal problems to worry about external, long-shot contacts. If they have a network at all, it is heavily weighted toward experts who can provide basic advice on running a business or managing the relevant technology.

As the business grows, it reaches the most vulnerable stage when it becomes mid-sized, and entrepreneurs at this stage need a contingency network to chart the course toward sustained growth. As Table 4.2 shows, these entrepreneurs make a special effort to build their networks.

Table 4.2[5]
Growth Stages and Personal Networks

The effect of firm size on the effort to build a personal network

Size of firm*	Distribution of entrepreneurs %	Distribution within each firm-size of effort to build a network: Special effort %	No effort %
Very small	4	75	25
Small	35	74	26
Medium	38	86	14
Large	17	59	41
Very large	6	100	-
Total	100	77	23

* Size categories are determined by the number of employees or the annual sales, with the former taking precedence if the two are not consistent.

Size	**Employees**	**Annual Sales**
Very small	less than 10	less than $2 million
Small	11-99	$2-$10 million
Medium	100-499	$10-$50 million
Large	500-2,499	$50-$250 million
Very large	more than 2,500	more than $250 million

Still later, once they become large, the successful companies acquire sufficient depth in their managerial structure that the level below the owner does most of the networking. Greater financial resources also enable the firm to spend a lot more money buying information through market research. The entrepreneur then becomes the synthesizer who paints the backdrop to strategic decisions and who can return to managing the internal affairs of the business. Finally, in the very large firms, the entrepreneur becomes the link to the world far beyond the specific affairs of the business and creates a vast personal network from all walks of life.

Because this study is focussed on successful entrepreneurs, it contains a weighting of very small firms that is far below that for all firms in Ontario and Canada. The results therefore reflect more established entrepreneurs. This does

[5] Ibid. Unpublished research from *The Entrepreneurial Edge*

not affect some overall averages, such as the proportion who make a special effort to build a network, because the smaller firms are close to the average of mid-sized, large and very large firms.

A critical part of personal networks is the choice of people who are in them. At start-up, the emphasis is inevitably on experts who can provide specific advice for the new venture — accountants, lawyers, bankers and people already in the same business. As Table 4.3 shows, suppliers, government people and business consultants rank much lower in importance at this stage.

Table 4.3[6]

Preferred Sources of Advice at Start-up

Percentage of owners who say they seek advice from the type of people shown when they start their business

Source of advice and/or information	Percentage who use the source of information %
Accountants	54
Lawyers	54
Someone in same business	47
Banks/financial institutions	45
Suppliers	37
Government	15
Business Consultants	10

As the business matures, the composition of the network changes. Fellow businesspeople become the most popular network targets. Entrepreneurs love to talk shop with people who can relate to their problems, even if they cannot provide all the answers. And they often come up with useful ideas.

As Table 4.4 shows, the second most popular people for the networks of successful businesses are customers. These people are rarely mentioned in start-ups, which naturally have few customers to speak of. However, almost half of the successful entrepreneurs include customers in their networks

[6] Ibid. *Newly-formed Small Businesses in Ontario, 1982-87*

— and they show more enthusiasm for these contacts than any other type. They often describe their customers as their best R&D or as the source of most of their ideas. Later, as a product line becomes established, the entrepreneurs reduce their contact with customers. About 60% of the small and very small firms cultivate their customers, compared to a third of the very large firms.

Table 4.4[7]
The People in the Networks, by Size of Business

Percentage of entrepreneurs in each size group who have in their networks the types of people shown

Type of network members	Total	Firm size*				
		Very small	Small	Medium	Large	Very large
	%	%	%	%	%	%
Businesspeople	90	100	84	100	77	83
Customers	44	75	58	32	38	33
Government	39	100	35	35	15	83
Suppliers	23	-	39	12	15	33
Professionals	22	50	23	18	8	50
Average number of network types	2.17	3.25	2.39	1.97	1.54	2.83

* Size categories are determined by the number of employees or the annual sales, with the former taking precedence if the two are not consistent.

Size	Employees	Annual Sales
Very small	less than 10	less than $2 million
Small	11-99	$2-$10 million
Medium	100-499	$10-$50 million
Large	500-2,499	$50-$250 million
Very large	more than 2,500	more than $250 million

Customers and businesspeople are the backbone of any network. At least one of them is present in every network. But there are other types of people the entrepreneurs choose, shown in Table 4.4 in order of popularity:

- Government people are especially popular among the

[7] Ibid. Unpublished research from *The Entrepreneurial Edge*

smallest firms, which look to them for basic advice and funding. Very large firms also court government contacts, both to keep on top of upcoming contracts and to stay close to the moving feast of government assistance programs. The firms in between are sufficiently independent that they can manage without government assistance and too busy to spend the time to acquaint themselves with what governments can offer them or to find out how to approach the task of getting it.

Suppliers can be an important source of industry information. They are privy to their industry's newest technological developments since they have to adapt their products accordingly. Often competitors are customers of the same supplier. Professionals are the least popular candidates for entrepreneurial networks. A professional can often give insights or ideas based on a thorough knowledge of the business, but many of them are not normally trained in the ways of business — and many entrepreneurs feel that an excellent professional often turns out to be a poor businessperson.

On average entrepreneurs have slightly more than two types of people in their personal networks, with the most enthusiasm coming from the very small and the very large firms. (As mentioned earlier, the weighting given to small firms in this study is less than the universe.) By contrast, the people who do not make a special effort to build networks cast their nets less widely — almost two-thirds of them limit themselves to just one type. These people virtually ignore government people, whereas almost half the networkers cultivate them. The only type that receives more attention from the people who don't make a special effort than from those who do make the effort is customers, who are in the networks of 67% of the former and 41% of the latter.

The Board of Directors

A director of a company is quite unlike any other member of an entrepreneur's personal network. For entrepreneurs, a board is an unparalleled source of inexpensive advice from people who should know their firms' affairs intimately. A board is therefore potentially the most powerful part of a personal network. But it can also be the bane of an owner's life. Active boards of

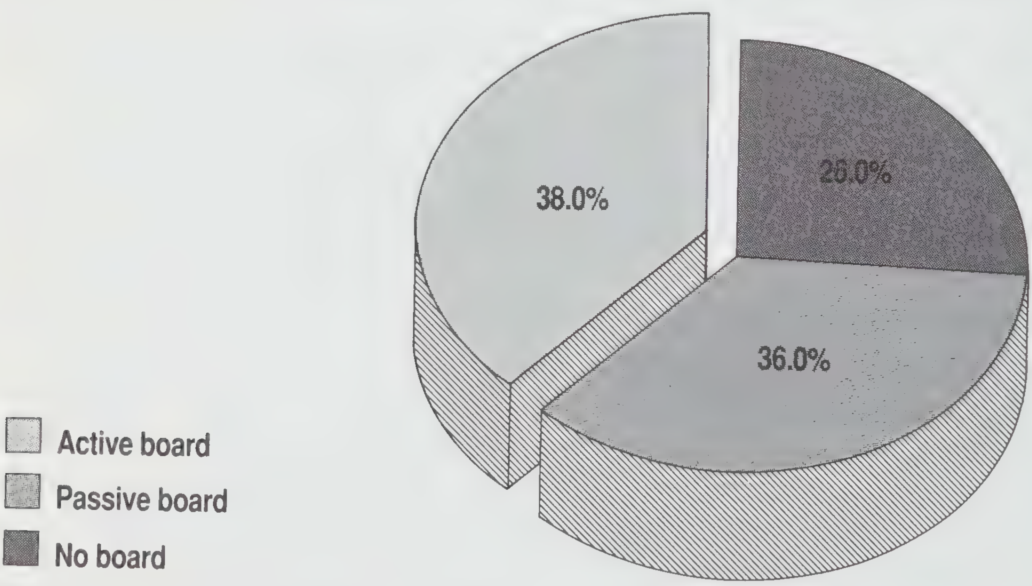
directors impose a discipline that forces entrepreneurs to articulate their strategies, at some risk they'll be found wanting. For some owners, this constitutes meddling by directors in affairs they don't fully understand and a potential hindrance to the entrepreneur's freedom of action that far outweighs the advantages of free advice and leads.

That's why so many smaller businesses dispense with boards of directors. As Chart 4.1 shows, more than a quarter of the entrepreneurs in this study have no board at all - and almost half the remainder have passive, rubber-stamp boards, made up mostly of employees. In this study of successful entrepreneurs, a mere 38% have active, effective boards of directors to whom they look for leads, advice and fresh perspectives.

Chart 4.1[8]

How Entrepreneurs Use their Boards, If At All

Percentage of successful entrepreneurs who have active boards of directors, passive boards or no board at all



[8] Ibid. Unpublished research from *The Entrepreneurial Edge*

The approach entrepreneurs adopt toward their boards of directors invariably reflects their attitudes toward taking advice in general. The ones who have active boards generally believe in seeking advice from their employees when they formulate their strategies and they draw business ideas from everywhere, as Table 4.5 shows.

Table 4.5[9]
How Entrepreneurs Use Their Boards of Directors

Distribution of entrepreneurs with no board, a passive board and an active board, by other traits that concern how they seek advice

Status of the board of directors	All owners	Distribution of types of board when: ideas for the business come mainly from the owner	others	employee participation in strategy formulation is significant	negligible
	%	%	%	%	%
None	26	36	6	17	55
Passive	36	42	26	36	35
Active	38	22	68	47	10
Total	100	100	100	100	100

It's particularly striking that almost all the entrepreneurs who have no board of directors believe they alone generate all the good ideas for their businesses. And when they do have a board, these independent-minded people keep them firmly in their place — only one-third of their boards are active, compared to almost three-quarters of the boards of the rest of the entrepreneurs. Similarly, more than half the entrepreneurs who keep their employees out of the strategy sessions reject the utility of a board entirely and only 10% of them run active boards.

As might be expected, very small firms are most allergic to directors — one-half don't have boards, compared to one-third for small and medium-sized firms, and none at all for the

[9] Ibid. Unpublished research from *The Entrepreneurial Edge*

large and very large firms. And when the very small firms do have a board, they are usually passive. For these firms, the imperatives of survival make leads and fresh perspectives irrelevant - they need professional help rather than friendly advice. As firms grow, however, active boards become more important. Almost all very large firms have them, although only half of the large firms in this sample have them.

Associations

The principal vehicles for finding the people to build networks are associations. Only a tenth of the entrepreneurs in this study built their networks without joining a single association. The rest have joined one or more associations of like-minded people, sharing common interests or objectives, as Table 4.6 shows. There are five principal types of associations that entrepreneurs join to further their business interests.

Table 4.6[10]
Entrepreneurs' Membership in Associations

Percentage of entrepreneurs who join given associations, by whether they make a special effort to build a network

Type of association	Entrepreneurs who belong to the associations shown and who: make a special effort to build a network %	do not make an effort to build a network %	Total %
Trade association	72	40	66
Community organizations	49	7	41
Other company boards	40	7	34
Charities	26	7	23
Entrepreneur groups	21	7	19
None at all	3	40	10
Average number of associations	2.08	.68	1.83

[10]Ibid. Unpublished research from *The Entrepreneurial Edge*

- By far the most popular, for obvious reasons, are the trade associations. Even if it's only to keep up with technological developments, most entrepreneurs pay their dues and go to industry meetings. Many go a lot further, acquiring a high profile through their trade associations. They're quoted in the press because they are on the executive, they meet all the leading players in the industry, they meet their counterparts in the same industry in other countries.

Generally, few well-established entrepreneurs are active in their trade associations. At a certain point, they phase themselves out of them, leaving it to their employees to keep in touch. They prefer to limit their involvement to specific areas they are particularly interested in. For a few entrepreneurs, trade associations are anathema. These people feel there is little they can learn from them and too much they can teach their competitors.

- The second most popular affiliations are community organizations, including Chambers of Commerce, export associations, local associations designed to promote some aspect of local industry (R&D for example) and local projects varying from an agricultural show to educational institutions. These organizations offer entrepreneurs access to a wide range of contacts from many industries and regions.
- A third of the entrepreneurs are directors on the boards of other companies. Intimate involvement in the challenges and problems of other people's businesses is in itself a learning experience, but these entrepreneurs also often derive an even greater benefit by embarking on quite separate ventures in partnership with their fellow directors. The camaraderie of these friendships is an important by-product, but the real pay-off is in their improved business acumen.
- Charitable organizations offer a marvellous opportunity to build relationships in an environment where the basis for co-operation is relatively easily established. The motivation here is much the same as belonging to community organizations, except that it is a great deal

more demanding on their time and the friendships formed in the course of performing their duties are usually more solid, mainly because they have shared so much more of themselves.

- Finally, there is a growing realization of the advantages of belonging to associations of entrepreneurs. The Canadian Federation of Independent Business led the way, putting entrepreneurs on the political map in this country. A splinter group later formed the Canadian Organization of Small Business, which is also a lobby group, although it has a greater proclivity for providing business advice to its members.

The newest generation of entrepreneur associations are more like mutual assistance groups. In an environment pioneered by the Young Presidents' Organization, they meet in small, local groups to discuss each other's problems and opportunities. There's no need to disclose too many pertinent details about their businesses, but members of the group have an opportunity to bounce specific ideas or problems off their usually empathetic colleagues.

The extent to which entrepreneurs use any of these five types of associations depends on their attitude toward networks. The people who do not make a special effort to build a network belong to few associations other than trade associations — and 40% of them belong to no associations at all, compared with 3% of entrepreneurs who do make an effort. On average the networkers belong to three times as many associations as the others.

CHAPTER 5
EMPLOYMENT CONDITIONS IN SMALL BUSINESS

Entrepreneurs do care about their employees, it would appear. In a recent survey conducted with the readers of Small Business Magazine, Ontario's owner-operators presented a picture of themselves as a thoroughly conscientious group. The responses to the "Best Bosses" survey[1] may not be representative of all small firms, because the 263 Ontario respondents averaged annual sales of $6.8 million and employed, on average, 51 full-time and 14 part-time people. But these companies have personnel management systems that would do most big companies proud.

And they are proud of it. They believe their employees would rate them 7.7 on a scale of 1 to 10, with 10 being an excellent boss. Other results of the survey include:

- More than half (56%) have written job descriptions for their employees, more than half of which were developed jointly between the supervisor and the employee;
- Almost three-quarters (72%) give their employees annual performance reviews. One-quarter prepare career plans for their employees;
- 92% have a policy to promote from within;
- The average pay increase last year was 8.8% and most of them (60%) also have bonuses, profit sharing or stock ownership plans; and
- They spend an average of 2.9% on employee training, most of which is for strictly job-related skills (although fully 30% said their training wasn't limited to job-related skills). A third also offer counselling for employees with personal problems.

The survey illustrates the lengths to which some

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[1] See *Small Business, The magazine for Canadian entrepreneurs*, November, 1989.

entrepreneurs are prepared to go to look after their employees. It may help dispel some of the myths about entrepreneurial management. Having said that, it's likely that most small businesses don't share the enthusiasm of these people for comprehensive human resource management systems.

Human Resource Management in Small Business

The Small Business Branch of the Ministry of Industry, Trade & Technology has looked into how small firms in Ontario manage people. In the first half of 1989, the branch undertook research on human resource management. This included a review of all available materials and services as well as a series of focus groups of owners of small and mid-sized firms. Also, the Committee of Parliamentary Assistants for Small Business went on a tour of seven cities in the province to seek out the views of small business owners and other affected institutions on training. This tour visited North York, Thunder Bay, Mississauga, Windsor, London, Niagara Falls and Ottawa and spoke with many small businesses and other relevant institutions, including representatives from the school system, government agencies, unions, banks and companies in the training field.

The preliminary findings of this research have been as follows:

- ***Benefits of training in management of human resources for owners and senior managers***
  Owners who have invested in training to improve their human resource management report they have enjoyed significant benefits. These firms told the Parliamentary Assistants they enjoyed lower staff turnover and developed better staff-management relationships as a result of the training. In some cases, product quality improved and direct financial benefits were obtained, such as a reduction in insurance premiums for delivery trucks, because drivers became more careful. Others found that supervisors who had been trained to provide appropriate discipline were able to extract greater efficiency from the workforce.

  The views of these firms are not shared by all small businesses, however. Even the focus groups, which were

composed of people who were positive toward human resource management, indicated there is little consensus on what human resource management is. Their understanding of the phrase usually centred on any one of recruitment, termination, orientation, development of people to increase efficiency and employee training. The last was the most common understanding.

Whatever this sphere of activity may be called, it doesn't rank high on the priority list of most managers of small firms until it's a crisis. Their knowledge of the subject is usually gleaned from casual sources — occasional books they have read, discussions with associates and counterparts in other firms, mentors, observations from their experiences on the job and, rarely, videos on the subject. Most owners and senior managers recognize that this knowledge base is inadequate for the motivation and management of their employees, but they are not inclined to do anything about it.

The Parliamentary Assistants also found that a major difficulty for small firms is that they don't have enough employees to allow one person to specialize in the function of human resource management. They therefore have to take someone off their current duties or, more often, ask a supervisor to do it in his or her spare time. These people have no formal training in human resource management.

Experts interviewed by the branch said that small firms start doing something about human resource management only when they suffer a severe labour shortage. And their response is usually ad hoc. Few of them make the connection between current labour shortages and the human resource issues they ignored previously. Another trigger that prompts attention to human resource management, according to the focus groups, is the sudden enlightenment of the owner or senior managers, who might suddenly decide they should do something about it. Often this is caused by an impending crisis or the firm reaching a size where it becomes imperative to organize the human resource management more formally.

The focus groups found that owners of small firms will

embark on an investment in human resource management only if they can recognize the potential for improving efficiency or the bottom line. This reticence is reinforced by the perception of many owners that their problems in recruiting and retaining their employees reflect the business environment, not their internal human resource management.

The Parliamentary Assistants found, moreover, that trained workers are often raided by other firms that do not train their own employees. Big firms, particularly, can offer better compensation and benefit packages than small firms, which makes it hard for them to keep the employees they have trained. Also, many have found it hard to replace the skilled workers in traditional fields when they have had to train them to work on computers.

There are significant regional variances in the problems encountered by employers in small firms. In Northern Ontario, for example, a lot of trained employees leave to go south, where they can find more opportunity with their new skills. This applies particularly when firms hire skilled labour from other regions of the province, so they find they have more success hiring local people and training them themselves. In Windsor, there are different problems, caused by the rapid pace of change in the automotive industry. Many firms in this region say technology is changing so fast, there's no time to wait for people to acquire new skills. Poaching skilled labour is a major problem in Windsor.

The employees themselves are perceived as being even less enthusiastic about training than the employers. The Parliamentary Assistants were told that few employees arrive on a new job with formal training, and any skills they do have are usually acquired through personal interest. Many of them don't think they need the training because they believe the current economic boom will go on forever and they don't want to invest in their own development. There is some concern that the culture of Canadian-born employees mitigates against the acquisition of skills on the job, because they are not accustomed to starting off in a lowly, unskilled position and working their way up to a skilled job. This is why

some employers prefer immigrants as employees.

Overall, the branch's internal research concludes that it is important for the future economic well-being of the province to promote the concept of human resource management to small businesses. It has to be carefully targeted to their needs, however. Once firms reach 75 employees, they start appreciating, without prompting, the importance of human resource management, so they do not need to be informed of the importance of the human resource management function. They need to know where they can acquire information on human resource management. These firms, employing 75-100 people in manufacturing or 20-100 in services, are the initial target group for government training programs. The more serious gap in Ontario, however, is in firms with 10 to 50 employees. These firms are so busy fighting to survive or dealing with an onslaught of crises, they seldom appreciate the need for human resource management, but they need it as much or more than bigger firms.

The major challenge is to persuade the owners of these firms they need help. Because so much of the materials and services currently available are too general to be of much specific use to small firms, there is little inclination to use them. The focus groups concluded that the best way to disseminate human resource management concepts would be through workshops or seminars followed by extensive one-on-one counselling. However, media blitzes and other more general approaches may also be needed.

- ***Effectiveness of existing institutions for human resource management***

The branch's internal investigation found many private and public sources of education in human resource management. Those offered by management consultants are often too expensive for small firms and therefore little used, although there are some notable exceptions. Many services are provided through trade associations or local chambers of commerce or small-business organizations, such as the Canadian Federation

of Independent Business (CFIB) and the Canadian Organization of Small Business (COSB). However, many of these programs are not designed for the specific needs of any particular small firm, so they are also not used enough. Owners and senior managers in small firms tend to use their informal networks to accumulate information about human resource management, but this is seldom sufficient for their needs.

The most accessible programs for small firms are provided by the education system, apprenticeships and government programs. The latter is discussed in the next section. This section deals with the first two.

The CFIB said its surveys showed that employers in Ontario, where unemployment is lowest, are more dissatisfied with the training services offered by both public and private institutions than are employers in any other province. Ontario's high schools also got the lowest ratings in the country.

Two themes emerged repeatedly, in the focus groups, the Parliamentary Assistants' tour and the branch's investigation, on the subject of the education system:

1. There is widespread agreement that the basic education system is central to the success of any form of post-secondary training. Unless basic education is improved, vocational training schools will always lag industry's and employees' needs. (For more on this, see the section later in this chapter titled "The training of young people entering the workforce").

2. Parents and teachers currently project a poor image of technical careers, thereby depriving industry of many people who would be better suited to technical trades than service jobs, particularly white-collar jobs.

It was suggested that vocational training opportunities should be promoted more actively in high schools, perhaps through the Career Counsellors. It was reported by an Ottawa-area school that its School Work Apprenticeship Program (SWAP) was working well. This program, modelled on the system in West Germany, prepares students for apprenticeship training, enabling

them to complete their apprenticeship requirements within a year or two of leaving school. The program has been approved by the Ministry of Skills Development.

The community colleges now play an important role in technical training, but they are often forced to work with inadequate resources, particularly in terms of qualified staff. They are also having some difficulties meeting the needs of small businesses, which don't always understand the role of the community colleges. The Parliamentary Assistants were told that small firms often confuse organizational problems with training problems.

The most severe criticism was reserved for apprenticeship programs. The Parliamentary Assistants were told there is a feeling among small firms that the Canadian apprenticeship programs are not as good as those in Europe because they don't provide students with enough basic skills. Others also felt that they restrict entry to their programs, sometimes excluding women, or demanding unnecessarily high educational qualifications. Some nonetheless felt that apprenticeships should be expanded to more trades to give them the opportunity to define their training needs.

- ***Federal and provincial government programs in human resource management***

  Some of the principal government programs that deal with human resource management include:

  - The Ontario Ministry of Skills Development (MSD) manages Skills Development Offices (OSDOs) across the province. These are storefront operations, designed to mesh with small-business needs.

    MSD has also staged an Introductory Level Human Resources Planning workshop free of charge. It was a one-day seminar, run by private consultants, who helped small firms to identify the costs and benefits of human resource management and made them aware of the additional resources available to help them in this area. The Ministry also sponsored a two-day Advanced Level HRP workshop, for a fee of $150, which explained how to install human resource

systems, using a personal computer, if appropriate. Responsibility for this program has been passed to the Ontario Training Corporation, which was created in 1988.

- The Federal Business Development Bank. The FBDB runs many courses and seminars, including seminars aimed specifically at recruiting and selecting personnel and human resource planning. The bank also runs the CASE program, which uses the skills of retired executives to counsel small firms on any matter, including human resource management.

  One of the most notable innovations at FBDB is the Community Business Initiative (CBI) program, which helps small firms help themselves. It was started in Orillia and Barrie in the fall of 1988 and is rapidly spreading all over the province and the country. The bank approaches a community to form an advisory committee, which assembles about 30 local businesspeople who are not competitors and invites them to participate in a 12-month program of mutual education in management.

  The program is led by a full-time program advisor, who arranges ten monthly sessions, each led by a skilled resource person. The participants share their experiences with each other in these sessions. Between group sessions, the advisor spends some time every month with each individual participant. Each small business spends a total of 80 hours in the program, 40 in workshops and 40 in one-on-one counselling.

  The role model for CBIs is the Northwest Enterprise Centre in Thunder Bay, which was initially funded partly by a grant from the Ministry of Industry, Trade & Technology (MITT). It now has 400 graduates.

- Employment and Immigration Canada (EIC). In its Canadian Jobs Strategy, EIC has a range of programs designed to help communities create and preserve businesses, subsidize training costs in approved institutions and contribute to the funding of new

projects. The department also subsidizes training costs for employees and small-business owners in its Skill Investment Program, as it does in its National Labour Market Innovations Program. It helps all businesses adjust to change through its Manpower Consultative Service and reimburses wage costs of employees sent to approved training institutions for up to two years. Finally, EIC sponsors, with the YMCA, Youth Enterprise Centres in nine cities across Canada.

EIC has also signed national human resource planning agreements with several major industrial and professional associations, aimed at matching the demand and supply of certain skills. And Regional Human Resource Planning Consultants co-operate with industry in planning for skills development.

In its investigation, the Small Business branch of the MITT found that OSDOs are extremely popular among small businesses. Their one-on-one approach is particularly successful. The main comment on the OSDOs is that they focus too narrowly on setting up programs — their clients would like to see them stay with them longer. The Parliamentary Assistants were told by OSDO managers that they are stretched too thin to perform a long-term training function. They can only aim to help small firms understand the benefits of training before they move on to the next client. The important step is to leave the clients with a structure for the further development of human resources. At that point, the clients worry less about the dollars.

A related comment arising out of the success of the OSDOs, but not part of the OSDOs' responsibilities, is that it now takes three months to get people into community colleges for training courses, compared to the four weeks it took previously. Other owners commented to the Parliamentary Assistants on the amount of paperwork required for MSD assistance. There must be some paperwork, of course, and the Ministry has kept it to a minimum, but it was suggested that MSD might consider a smaller package

to upgrade a small firm's training program, without overhauling it.

In general, small-business owners are favourably inclined toward government initiatives in human resource management, according to the focus groups. Since the governments do not have a profit motive, the owners believe they will obtain good value for money. However, there was some debate over whether this is appropriate and concern at the likely level of paperwork.

- **The Training of Young People Entering the Workforce**

  The problems, mentioned earlier, of perceived inadequacies in the basic education system are reflected in the uneasy transition of high school leavers into the labour force. A recent study by the MSD examined 1,400 young Ontarians aged 17 to 28 who either left high school or intended to leave high school without pursuing any further education. These account for about two-thirds of all high school leavers, split equally between those who completed their secondary school education and those who dropped out of school. Their reasons for not pursuing further education were primarily that they needed the money (46%) or they perceived barriers to further education, such as discouragement or personal reasons (34%). Another 28% rejected the utility of further training. And 12% expected to return to their studies after taking some time off.

  Only 13% of these young people received any career counselling at school, none of it from their high schools. Although all of these students went straight into the labour force (or intended to, in the case of the students still at school), more than half of them did, in fact, receive further training after they left school. Of those who did receive further training, two-thirds had only job-related training, while the balance pursued further training out of personal interest.

  Many of these school leavers did, in fact, return to post-secondary educational institutions, as Table 5.1 shows, but many would have preferred not to have been

limited to on-the-job training. Only 39% actually went to community colleges or university, but 78% would have preferred to do so.

Table 5.1[2]
What School Leavers Would Like and What They Get

Among school leavers who did not anticipate further education when they left high school, a comparison of the sources of further education they actually got and the sources they would have preferred

Sources of further education and training	Actual sources %	Preferred sources %
Community College	37	59
On-the-job training	24	7
Apprenticeship	12	3
Private college	8	4
Correspondence course	2	2
University	2	19
Government training	-	2
High school	-	2

The study uncovered a major motivation in pursuing post-secondary education — insecurity of employment. Among the young people in the sample who felt secure in their jobs, a third were very interested in acquiring new skills, compared to two-thirds for those who did not feel secure.

Legislative Initiatives

The government is committed to promoting employment equity. Employment equity is a process that will provide a framework for the progressive integration into all areas of the workforce those groups that are either disadvantaged or minorities. The final form was not determined when this report was printed, but there appear to be two options:

- Option one involves persuading broader public and private sector employers to undertake employment equity

[2] Pathways, a study of labour market experiences and transition patterns of high school leavers, conducted by Decima Research for the Ministry of Skills Development, 1989

for a number of disadavantaged groups on a voluntary basis. With this approach, the government would provide inducements to employers; and

- Option two would be to regulate the implementation of employment equity through the introduction of mandatory legislation or comprehensive programs such as contract compliance.

As this report was written the government was consulting interest groups about these two approaches. Groups being consulted include: the designated groups (women, minorities, disabled persons and aboriginal people), business associations, labour organizations and public sector employers.

The government will also be amending legislation governing working conditions to reflect changes to the Unemployment Insurance Act. This will affect pregnancy leave and paternity leave, among other things.

Payroll Taxes

Employers are currently required to pay the federal and provincial governments three taxes which are levied on payroll — for Unemployment Insurance (UI), Canada Pension Plan (CPP) and the Workers' Compensation Board (WCB). From January 1, 1990, a fourth has been added in Ontario — the Employer Health Tax (EHT), which will replace premiums formerly paid to the Ontario Health Insurance Plan.

The EHT is not levied on about a quarter of a million Ontarians who are sole proprietors. These people benefit because they are no longer paying premiums for the Ontario Health Insurance Plan ($357 a year for individuals, $714 for families), and they are not required to pay the EHT. For small firms with employees, the EHT will cost 0.98% of payroll if their total payroll is less than $200,000 or 1.95% of payroll if their payroll is more than $400,000. Firms with payrolls of $200,000 to $400,000 will pay a graduated rate. In 1987, there were more than 304,000 enterprises with employees in Ontario, of which 298,000 (98%) were small firms employing fewer than 100 people. The average payroll for these small firms in 1987 was $118,000 and the average number of employees was 5.4. About 80% of small businesses in Ontario

will therefore pay an EHT of 0.98% of payroll.

The effect of the EHT, along with expected increases in the other payroll taxes, on small businesses (assuming they pay the EHT at 0.98%) will be to raise payroll taxes 25% in 1990, to $2,258 per employee, from $1,807 in 1989. In 1983, the total payroll taxes per employee paid by small businesses was $1,091. As Chart 5.1 shows, the EHT will account for about 10% of the total payroll taxes in 1990.

The net impact of this increase in payroll taxes on small businesses is difficult to assess. Small firms are more labour-intensive and they are the primary creators of new jobs, so they will pay a disproportionate share of the higher level of payroll taxes. However, a great deal depends on whether they have been paying all or part of the OHIP premiums for their employees. A firm with high salaries that has not been paying OHIP premiums for its employees will be subject to a sharp increase in payroll taxes, but a firm with low average salaries that has been paying OHIP premiums in full for its employees will be better off. In a small firm, an employee earning about $36,000 will require an EHT of $353, or about the same as the $357 OHIP premium for individuals. So, employers who paid their employees' OHIP premiums and have an average wage of less than $36,000 are better off.

It's not known how many small firms paid their employees' OHIP premiums, but previous studies[3] have shown that all or part of the OHIP premiums were paid by 22.5% of firms younger than three years and 83% of manufacturing firms with 50 to 200 employees. The Canadian Federation of Independent Business has also conducted a study in which it found that 43% of its members paid all or part of their employees' OHIP premiums in 1983. About 70% of all OHIP premiums are paid by employers, small and large. It therefore seems likely that a little less than a half of small firms were paying all or part of their employees' OHIP premiums, so the impact of the EHT on them will be reduced accordingly.

The EHT is not the only factor in the rapid increase in

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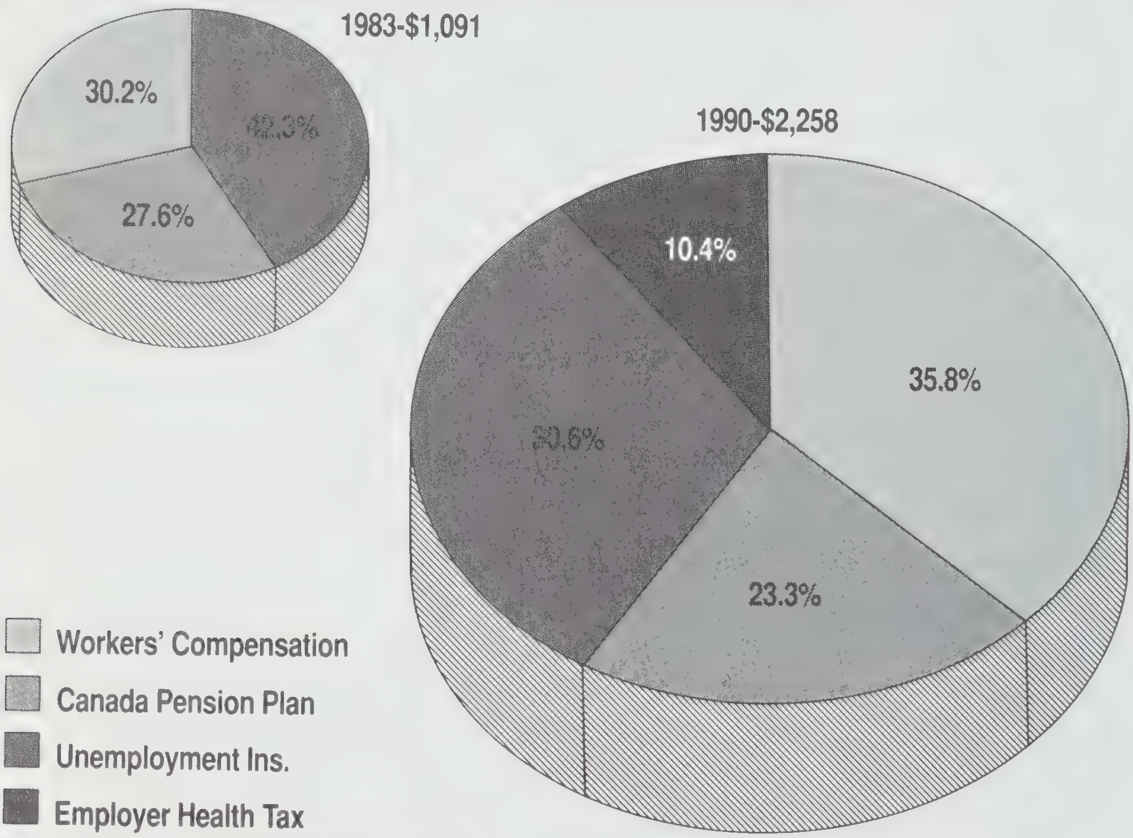
[3] Small Business Payroll Taxes, 1987, prepared by the Small Business Branch of the Ministry of Industry, Trade & Technology, March, 1987.

Chart 5.1[4]
The Payroll Tax Load, 1983-90*

Each payroll tax expressed as a percentage of total payroll taxes**



* The taxes for 1990 are estimated on the assumption that CPP and WCB continue their traditional rates of increase and that UIC premiums will return to their 1988 levels as a result of changes introduced in the 1989 federal budget. The EHT is assumed to be the minimum of 0.98% of payroll.

** This does not take into account any savings to employers who had been paying OHIP premiums for their employees.

[4] *Internal research, Ministry of Industry, Trade and Technology, based on data from Canada Employment and Immigration, Workers Compensation Board of Ontario and Statistics Canada, Small Business and Special Surveys.*

payroll taxes. WCB premiums have risen so dramatically since 1983, that they have increased their share of total payroll taxes despite the addition of the EHT. This has meant that UI and CPP have reduced their share of total payroll taxes, despite a significant increase in dollar terms. UI and CPP account for about 50% of payroll taxes in 1990, compared to 70% in 1983.

The combined payroll taxes will amount to 8.7% of payroll (including payroll taxes) in 1990, compared to 5.9% in 1983, as Chart 5.2 shows. Workers' Compensation will rise to 3.1% of payroll from 1.8% of payroll in 1983. UI premiums decreased in 1989 to 2.6% of payroll thanks to a surplus in the premium account after six years of economic growth, but are expected to return at least to 1988 levels in 1990.

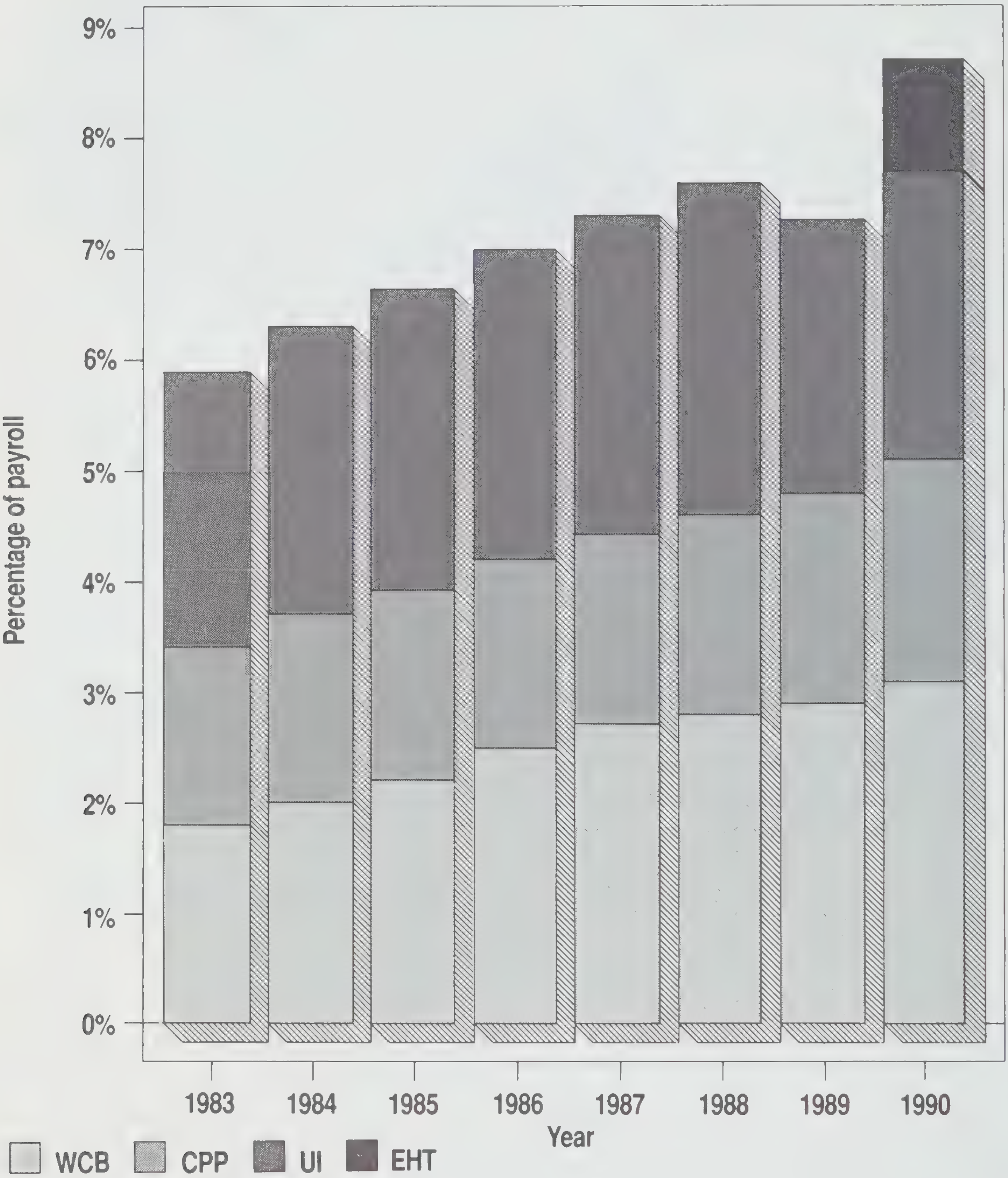
The average annual increase in payroll taxes from 1983 to 1990 will have been 11%. During 1983 to 1989, the annual growth rate was 8.8% for all payroll taxes, compared to 4.6% for wages and salaries, 4.7% for inflation and 5.5% for real Gross Provincial Product.

Table 5.2 demonstrates the extent to which the increases in WCB premiums have exceeded other payroll taxes, with an average annual increase of 13.7% a year between 1983 and 1990. WCB payments hit hardest in construction and manufacturing firms, which are estimated to pay $2,933 and $969 per employee in 1990 respectively, bringing their total payroll taxes per employee to $4,467 and $2,427 respectively.

Chart 5.2[5]

Component Taxes as a Percentage of Payroll[6]

Each payroll tax expressed as a percentage of total payroll (including payroll taxes), 1983-90



[5] Ibid.

[6] The payroll of small businesses is assumed to be based on an average wage equal to 86% of the average industrial wage for all workers. The average industrial wage for 1989 and 1990 is assumed to be the 1988 average industrial wage plus the appropriate increases in the Consumer Price Index.

Table 5.2
Average Annual Increases in Payroll Taxes, for Selected Industries

Average annual increases between 1983 and 1990, for a selection of industries, for each payroll tax and all payroll taxes

Type of tax	Industry				
	Garages	Rest-aurants	Manufac-turing	Constr-uction	All industries
	Average annual increase in taxes, 1983-90				
	%	%	%	%	%
Unemployment Insurance	5.7	5.9	6.0	6.0	6.0
Canada Pension Plan	8.4	8.5	8.4	9.7	8.3
Workers' Compensation	14.6	17.8	15.1	14.1	13.7
All payroll taxes	10.8	11.2	11.6	12.8	11.0
	Average payroll taxes per employee, 1983 and 1990				
1990 payroll taxes ($)	$1,998	$824	$2,427	$4,467	$2,258
1983 payroll taxes ($)	$972	$391	$1,125	$1,924	$1,091

PART II

The Economic Impact of Small Business

CHAPTER 6
SMALL BUSINESS IN ONTARIO

The 1981-82 recession marked the beginning of the small business revolution. Before that, big business dominated the minds of the economic planners, because they created jobs in multiples of a thousand, they made all the major investments and set the pace for small firms to follow. Since the recession, a strange thing happened. Small firms became the front-runners in job creation, steadily levering their importance from an equal share with big business at the end of the 1970s to a 90% share by 1987.

Ontario is, of course, the major centre for big business in Canada and has benefitted greatly from the powerful firms that have made their home in the province. But even in Ontario, small firms create 75% of the jobs and they are growing at seven times the rate of big firms. This is changing the face of the labour force rapidly. Small firms now employ 33% of total labour force, or 39% of the private-sector workers. Across Canada, small firms now even employ more than the big firms with more than 500 employees. Ontario's big firms still employ more than the small firms, but that gap is disappearing fast, too.

The small business phenomenon is driven by new ventures, which accounted for about 95% of the new jobs created in Ontario during 1978-87. This rush of entrepreneurs is giving the economy a different feel. More than 90% of the province's 300,000-odd firms employ fewer than 20 people and their average number of employees is 4.4. That makes for an awful lot of very small businesses. But these people are maturing as entrepreneurs and beginning to grow rapidly. The average size of Ontario's firms has fallen three percentage points in the past nine years, to 15 employees per firm. If governments and their agencies are excluded, the average firm size is only 13. (In the rest of Canada, it's nine.)

Ontario's big firms have, of course, continued to perform well — and far better than big firms elsewhere in the country. But their growth rates pale beside those of small firms.

Between 1978 and 1987, small firms in Ontario increased their employment by 69%, compared to 50% elsewhere in Canada and 10% in Ontarian big firms. Before the recession, one-third of the employment growth in small firms was in Ontario. Now it's 45%. And some of the growing small firms are remarkable. A small group of 1,500 firms that grew particularly fast accounted for 20% of all new jobs created in the province between 1978 and 1987. Not bad for 0.72% of the firms in the province. These people at the cutting edge hold our hopes for future employment.

The interesting thing is that it appears small firms are now setting the economic pace. When they are strong, the whole industry is strong — including big business. It appears that the more big businesses dominate an industry, the worse its employment growth rate is.

The big stars of job creation are personal and business services, community services and retail trade. These three together accounted for 60% of the new jobs in Ontario between 1978 and 1987. The power behind these are two stellar industries — services to business and health and welfare. The former is growing at 7% a year in Ontario, far outpacing any other industry. In small firms in this industry, employment is growing at 10% a year. Health and welfare also grew fast. Traditionally an industry dominated by big businesses like hospitals and welfare agencies, the employment action in health and welfare lately has been in small firms — nursing homes, medical clinics and so on. Employment growth for the whole industry during the nine years to 1987 was slightly more than 4% a year, but in small businesses, it was an impressive 8%.

These industries typify what's happening with small business. Even in the automobile industry, the home of giantism, small firms are doing very well, growing at 10% a year, while the big firms keep their employment about the same. Electrical and electronic products is another star in Ontario. While the big firms in this industry are actually shedding labour, the small firms are growing at 9% a year.

Ontario has always had strength in big business as the head office capital of Canada. It has also benefitted from having an overwhelming concentration of the employment in the booming auto industry, which has spread its benefits into

many parts of the manufacturing industries. The auto industry is volatile, however; greater long-term strength in Ontario may lie in industries like the media, printing, electronics, furniture, services to business, food and beverage and health and welfare. These are the industries where the growth has been strong and Ontario companies have highly developed expertise.

It is nonetheless a time of great change that is wrenching the economic fabric as we try to adjust to fit the new world. The turmoil in the world of employment is nothing short of astonishing. Not everyone understands the role of small business, but there is no denying it.

The Small Business[1] Fact Sheet[2]

All Employers	Ontario	Canada
Number of firms, 1986[3]		
Total	290,260	851,492
In small firms	284,066	840,694
Small firms as a % of total	97.9%	98.7%
Increase in number of firms, 1978-86		
Total	74,737	250,664
Small firms	73,887	249,033
Small firms as a % of total	98.9%	99.3%
Average growth rate p.a. for big firms	1.9%	2.1%
Average growth rate p.a. for small firms	3.8%	4.5%
Number of jobs[4], 1986		
Total (000s)	4,381.6	10,776.1
In small firms (000s)	1,456.7	3,904.1
Small firms as a % of total	33.2%	36.2%
Net gain in jobs, 1978-87		
Total gain (000s)	1,021.1	2,042.9
Total percentage increase over period	29%	22%
Gain in small firms (000s)	765.7	1,736.3
Percentage increase in small firms	69%	57%
Share of small firms in total	75%	85%
Average growth rate p.a. in big firms	1.1%	0.5%
Average growth rate p.a. in small firms	6%	5%
The big winners		
Share of total employment growth in:		
Personal and business services	28%	31%
Community services[5]	16%	21%
Retail trade	16%	19%
Small-business share of employment growth in:		
Personal and business services	75%	81%
Community services	42%	48%
Retail trade	73%	78%

1 Small business is defined as those with fewer than 100 employees
2 Source: Statistics Canada, Business Microdata Integration and Analysis and Small Business & Special Surveys
3 The 1987 statistics are not accurate for the distribution, by size of firm, of employment or number of firms. The 1986 statistics are accurate in this regard, so they are used wherever size distributions are involved.
4 Full-time equivalent jobs (part-time jobs count as a fraction of a full-time job)
5 Community services includes health & welfare, education and non-profit cultural institutions

The Market[6] Sector	Ontario	Canada
Number of firms, 1986		
Total	262,889	773,479
In small firms	257,541	765,112
Small firms as a % of total	98.0%	98.9%
Increase in number of firms, 1978-86		
Total	67,204	227,028
Small firms	66,405	225,824
Small firms as a % of total	98.8%	99.5%
Average growth rate p.a. for big firms	2.0%	2.0%
Average growth rate p.a. for small firms	3.8%	4.5%
Number of jobs, 1986		
Total	3,415.8	8,059.0
In small firms	1,336.8	3,533.3
Small firms as a % of total	39.1%	43.8%
Net gain in jobs, 1978-87		
Total (000s)	739.7	1,418.6
Total percentage increase over period	26%	20%
In small firms (000s)	694.5	1,515.3
Percentage increase in small firms	68%	54%
Job gains in small firms as a % of total	93.9%	106.8%
Average growth rate p.a. in big firms	0.3%	-0.3%
Average growth rate p.a. in small firms	5.9%	4.9%

[6] The market sector is defined as all industries other than those funded by governments or their agencies. The funded sector includes public administration, health and welfare, education and religion.

The Self-Employed[7]	Ontario	Canada
Number of self-employed people, 1986		
Total (000s)	408	1,209
Percent who are women	24%	22%
Increase in self-employed, 1981-86		
Total (000s)	50	114
Percent increase	14%	10%
Increase in self-employed women	27%	27%
Increase in self-employed men	10%	6%
Women's share in total increase	42%	49%
Average earnings, 1986		
Self-employed (incorporated)	$37,461	$33,435
Self-employed (unincorporated)	$27,190	$24,313
Employees	$21,317	$20,272
Age distribution, 1986		
Average age:		
self-employed men	44.6	44.2
self-employed women	42.2	41.6
all self-employed	44.0	43.7
employees	36.4	36.0
Percent aged less than 25:		
self-employed	4%	4%
employees	23%	23%

[7] Source: 1986 census, Statistics Canada

CHAPTER 7
SMALL BUSINESS AND JOB CREATION

Between 1978 and 1987, small firms, which are defined as those employing fewer than 100 people, accounted for 75% of the jobs created in Ontario. The figure is even more impressive for Canada, where small firms were responsible for 85% of the increase in employment[1].

This phenomenon is now well-known, although it is still a relatively recent trend. It started during the recession of 1981-82, which precipitated a rash of corporate lay-offs across Canada in 1982 and 1983. Although these cutbacks were severe, reducing the employed population by more than 5%, they barely touched small firms, which dropped their employment by a scant 46,000. This represents less than 8% of the total jobs lost during those two years and only 1.4% of the total employment in small firms.

Before the recession, small firms accounted for about 55% of the jobs created in both Canada and Ontario. Immediately after the recession, in 1984 and 1985, they accounted for two-thirds of the new jobs in Ontario, three-quarters in Canada. And the trend is accelerating. The most recent year for which statistics are available is 1987 and it is now apparent that the trend toward small business is gathering steam. In 1986 and 1987, small firms accounted for almost 90% of the jobs created in Canada, and three-quarters in Ontario. As Chart 7.1 shows, the gap between the jobs created by small firms and big is widening quickly.

The movement toward small firms reflects the combined effects of several trends. Some of them are sociological, as people choose more and more to be their own bosses (see Chapters 2 and 3). Some are economic, as the economy shifts out of manufacturing and into services (see next chapter).

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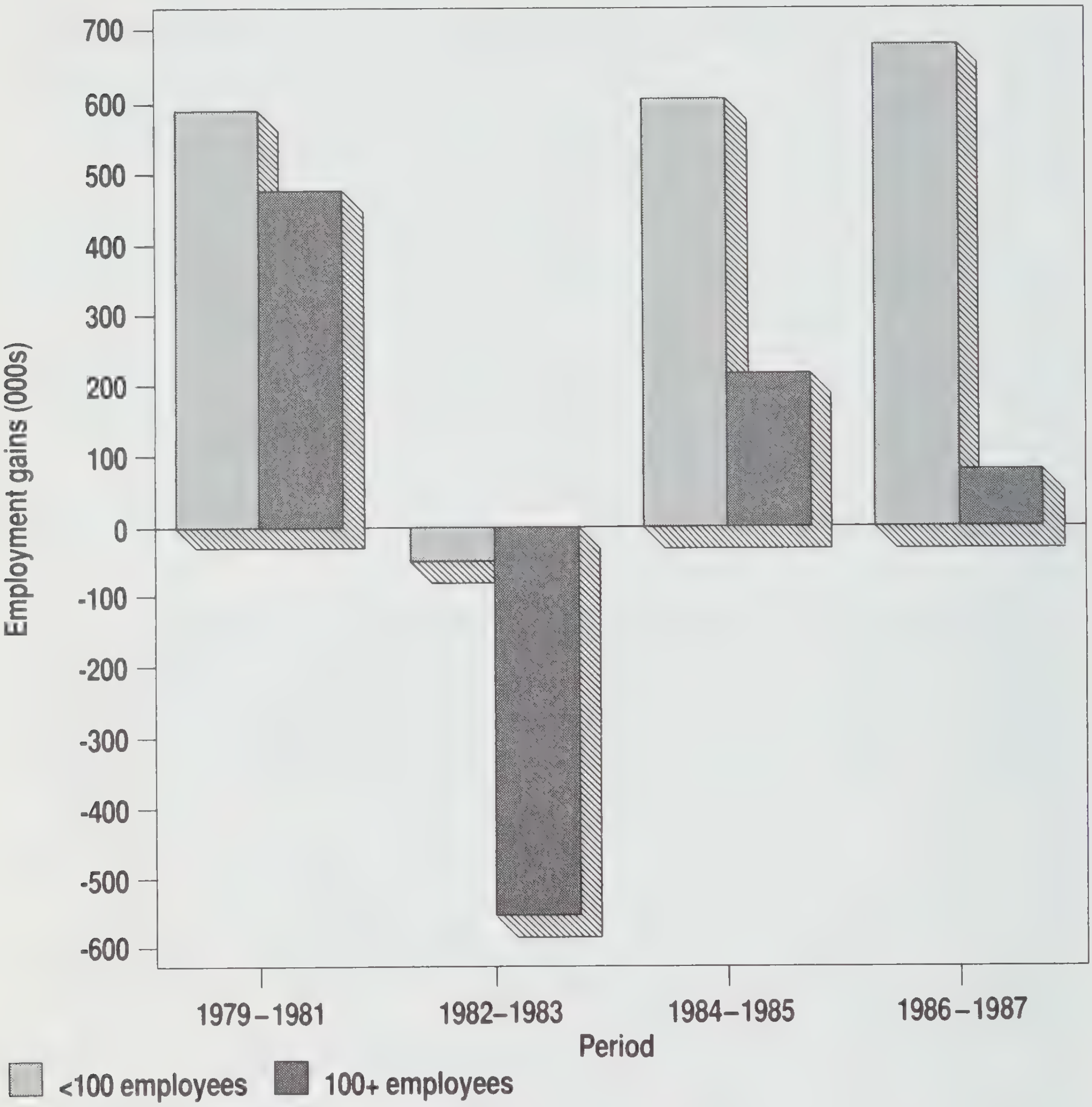
[1] All the statistics in this chapter come from Statistics Canada, through the *Business Microdata Integration and Analysis and Small Business & Special Surveys*.

Chart 7.1
The Growing Role of Small Firms in Job Creation

Gains in Canadian employment, by size of firms, in the four economic stages of the period 1979-87



This encourages small firms because manufacturing requires large investments to start a firm, while service firms can be started with very small investments. And some are corporate, as the large firms move to meet international competition by slimming down their overheads in a massive downsizing exercise that has not yet run its course.

It is tempting to suggest that the recent rash of corporate takeovers will reverse the downsizing trend, but it is more

likely that it will breed a second surge of downsizing a few years down the road. The latest available data is for 1987, which was too early to catch the effects of the takeover binge, but it's reasonable to assume that the big takeovers will not create many new jobs. Their most likely effect will be to accelerate the rise in the importance of small firms in creating new jobs. They will probably increase the average size of the biggest firms, without disturbing the overall distribution of employment between the different sizes of business.

The steady accumulation of new jobs in small firms is changing the distribution of employment rapidly. As Table 7.1 shows, between 1978 and 1986, small firms in Canada increased their share of total employment more than two and a half percentage points to 36.2% from 33.5%. The biggest firms, employing more than 500 people have seen their share of employment shrink a matching two and a half points to 48.4% from 50.9%. Mid-sized firms have fallen marginally to 15.4%.

Table 7.1
Where the Jobs Are, and Have Been in Canada

Distribution of employment, by firm size in 1978 and 1987, and distribution of the jobs created in the intervening years

Number of employees in the firms	Employment distribution 1978		Share of new jobs created 1979-87		Employment distribution 1986*	
	(000s)	%	(000s)	%	(000s)	%
Fewer than 5	619.9	6.8	1,034.1	50.6	839.6	7.8
5 - 19	1,013.5	11.1	459.1	22.5	1,308.1	12.1
20 - 49	805.3	8.8	166.1	8.1	1,003.1	9.3
50 - 99	619.9	6.8	77.0	3.8	753.3	7.0
Small firms	**3,058.6**	**33.5**	**1,736.3**	**85.0**	**3,904.1**	**36.2**
100 - 499	1,431.5	15.6	153.2	7.5	1,660.2	15.4
500 or more	4,650.9	50.9	153.4	7.5	5,211.8	48.4
All firms	**9,141.0**	**100.0**	**2,042.9**	**100.0**	**10,776.1**	**100.0**

* Note. The new jobs created by firms with fewer than 5 employees during 1979-87 exceed the total jobs in that category in 1986. This is because many of them grew into bigger categories and were therefore no longer counted as having fewer than 5 employees. But they were in the smallest category in 1978 or when they started business during 1979-87.

The most important contribution to job creation has come from firms employing fewer than 20 people. More than half of all new jobs have come from firms employing fewer than five people, which accounted for 7.8% of total employment in 1986, compared with 6.8% in 1978.

The trends have been similar in Ontario, although Ontario has had, for many years, a much stronger presence in big firms than has the country as a whole. Nevertheless, as Table 7.2 shows, small firms have increased their share of total employment in Ontario by almost two and a half percentage points over the eight years to 1986.

Table 7.2
Where the Jobs Are, and Have Been in Ontario

Distribution of employment, by firm size in 1978 and 1987, and distribution of the jobs created in the intervening years

Number of employees in the firms	Employment distribution 1978		Share of new jobs created 1979-87		Employment distribution 1986*	
	(000s)	%	(000s)	%	(000s)	%
Fewer than 5	214.7	6.0	388.6	38.1	284.6	6.5
5 - 19	366.7	10.3	209.9	20.6	472.1	10.8
20 - 49	295.8	8.3	96.6	9.5	391.1	8.9
50 - 99	228.2	6.4	70.6	6.9	308.9	7.0
Small firms	**1,105.4**	**30.9**	**765.7**	**75.0**	**1,456.7**	**33.2**
100 - 499	531.6	14.9	102.3	10.0	679.4	15.5
500 or more	1,936.9	54.2	153.1	15.0	2,245.5	51.2
All firms	**3,573.9**	**100.0**	**1,021.1**	**100.0**	**4,381.6**	**100.0**

* Note. The new jobs created by firms with fewer than 5 employees during 1979-87 exceed the total jobs in that category in 1986. This is because many of them grew into bigger categories and were therefore no longer counted as having fewer than 5 employees. But they were in the smallest category in 1978 or when they started business during 1979-87.

Following established patterns, Ontario's big firms played an important part in job creation, accounting for 15% of the new jobs during 1978-87, which is twice the rate for Canada. Even this understates the situation, however, because Ontario has a disproportionate share of big firms. In fact, Ontario accounted for 100% of the growth in employment in

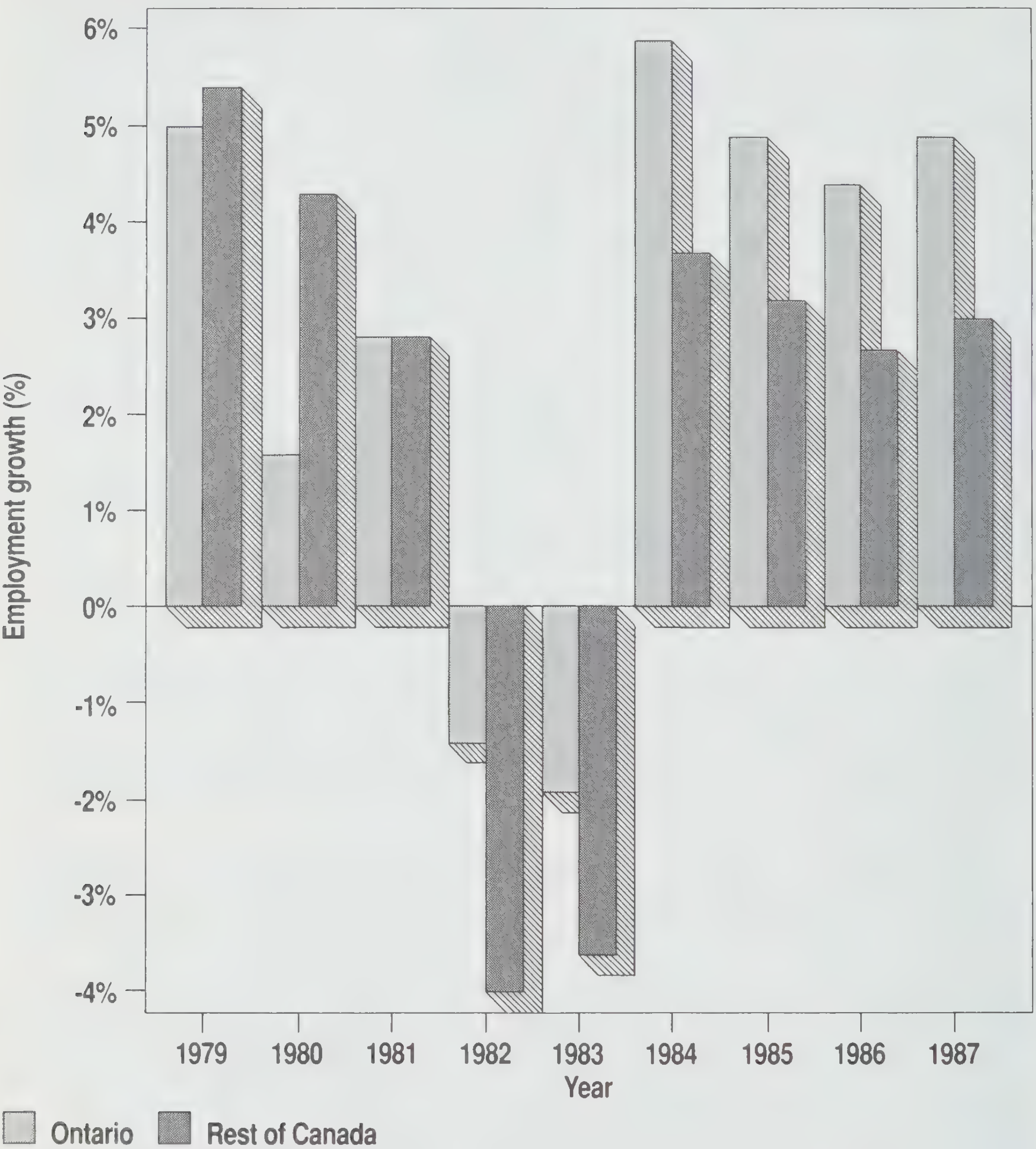
firms employing more than 500 people in Canada. In the rest of the country, employment levels in these firms were the same in 1986 as they were as in 1978.

Ontario's strength was not confined to the big firms, however. The larger small firms and the mid-sized firms have also done appreciably better in Ontario than in the rest of the country. Firms employing 20 to 499 people accounted for 26% of the job creation in Ontario, compared with 19% in Canada. The quid pro quo was, of course, the smallest firms (employing fewer than five people), which accounted for only 38% of job creation in Ontario, compared to more than 50% in Canada. (If Ontario is excluded, these firms accounted for 63% of the new jobs during the same period in the rest of Canada.) This strength in the mid-sized firms has meant that, even though Ontario's big firms made a bigger contribution to job creation, their share of total employment fell faster than it did in Canada. Their share of employment fell three percentage points over the period to 51.2%.

All this reflects the powerful growth that has lifted Ontario's economy to dominant heights within Canada since the recession. Before 1982, Ontario had lagged the rest of the country by a significant margin for several years. After 1982, as Chart 7.2 shows, annual growth in employment has never been less than 1.7 percentage points higher in Ontario than in the rest of the country.

Overall, employment grew 29% between 1978 and 1987 in Ontario, which is the equivalent of an annual average growth rate of 2.8%. The rest of Canada lagged far behind with a total increase of 18%, equivalent to an annual rate of 1.9%. The larger firms, of course, grew more slowly than this, but the gap between Ontario's performance and that of the rest of the country was even wider among big firms than among small ones. Mid-sized firms, employing 100 to 499 people, grew by 19% in Ontario and 6% in the rest of the country, while the biggest firms (employing more than 500 people) grew 8% in Ontario during these nine years, while they did not grow at all in the rest of Canada. (Chart 7.3)

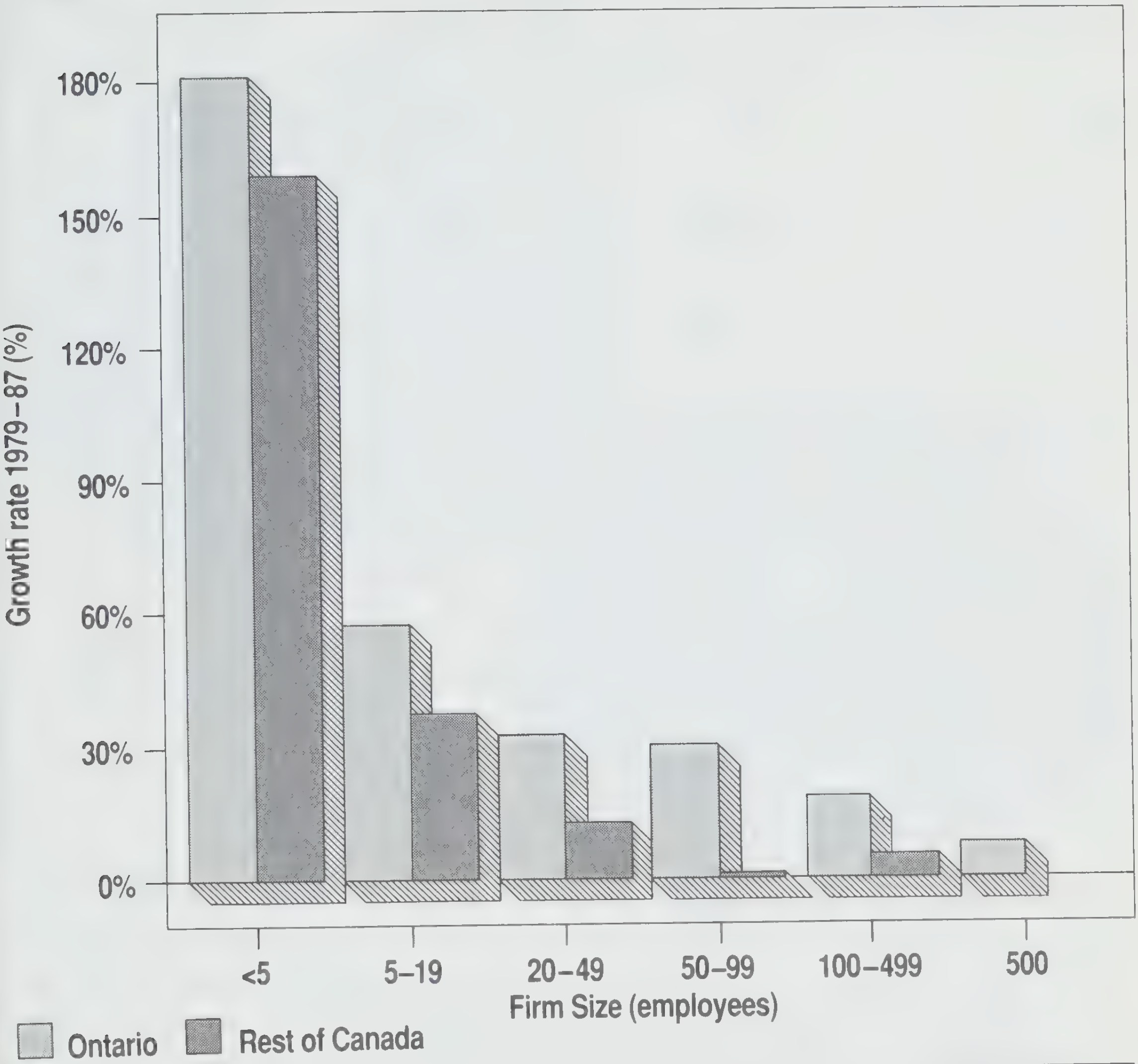
Chart 7.2
Comparison of Employment Growth in Ontario and the Rest of Canada



Because of Ontario's strong overall growth, however, this significant imbalance in the growth of larger firms was not at the expense of small firms. Small firms in Ontario increased their employment by 69% during the nine-year period, which is the equivalent of an annual rate of 6%. The rest of the country increased employment in its small firms by 50%, or 4.6% a year.

Chart 7.3
The Smallest Firms Grow Fastest

Growth rates during 1979-87, by size of firm, for Ontario and the rest of Canada



The result is that even Ontario has become more small-business minded. With 36% of the small-firm employment in Canada in 1978, it generated 44% of the new jobs in small firms during 1978-87. Table 7.3 shows how Ontario has increased its share of small-business jobs since the recession, just when small firms all over Canada were increasing their share of total job creation. At the same time, by 1986-87, Ontario's big firms were creating jobs while the rest of Canada's were diminishing their jobs in firms employing more than 500 people. By 1986, Ontario had raised its share of Canadian employment to 41% from 39% in 1978.

Table 7.3
The Job Powerhouse in Ontario

Ontario's share of Canadian job creation in small firms and other firms

	New jobs created in:				Ontario's share of total job creation in firms that are	
	small* firms		big* firms			
Period	Ontario	Rest of Canada	Ontario	Rest of Canada	small*	big*
					%	%
1979-81	188.4	405.8	162.0	320.9	32	34
1982-83	15.0	-61.0	-145.5	-405.9	n/a	n/a
1984-85	271.1	335.3	150.8	72.6	45	68
1986-87	300.9	373.4	96.3	-11.4	45	113
Total**	765.7	970.6	255.4	51.2	44	83

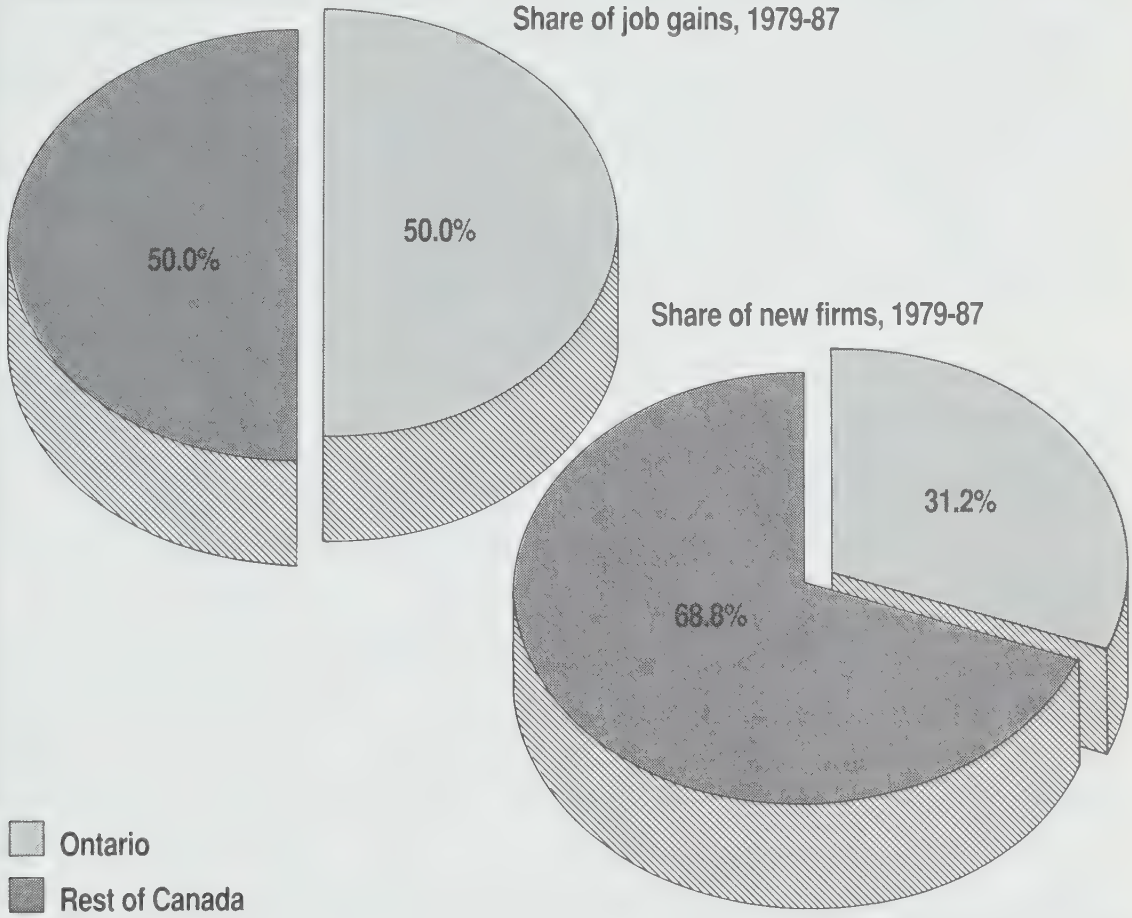
* Small firms are those with fewer than 100 employees
** Figures may not add up due to changing classifications

The major force behind the strong performance of small firms has been, of course, new ventures (see The Start-up Revolution, Chapter 2). One indication of this is that the number of firms is growing more quickly than the number of employees. In Canada, the number of firms in 1987 was 47% more than in 1978. Over the same period, employment grew 18%. As Chart 7.4 illustrates, the divergence was not as marked in Ontario, where the number of firms grew 41% over the same period, while employment advanced by 28%.

This is a sign of a maturing entrepreneurial economy. In a less mature entrepreneurial economy, the growth in jobs has to come from new entrepreneurs, who start and lose businesses in quick succession until they build up an adequate local infrastructure for business and personal development. As the new entrepreneurs acquire momentum, they make fewer mistakes and they create more lasting jobs — and employment growth comes with fewer additional firms. This phenomenon is also behind the strength of the mid-sized firms in Ontario, which can prosper only when there is an infrastructure to nurture the entrepreneurs capable of leading small firms through the transition to mid-sized firms.

Chart 7.4
Ontario Needs Fewer Firms to Grow More

Ontario's share of growth in the number of firms and in the number of jobs during 1978-87



Still, new businesses are being formed at a torrid pace, having raised the total number of businesses in Canada to 851,492 in 1986 from 600,828 in 1978. Small firms raised their share of the total number of firms by a very small amount, to 98.7% from 98.5%. However, there was an important shift within the ranks of small firms. Those employing fewer than five people raised their share of total firms to 75.9% from 74.4% between 1978 and 1986, while the shares of the larger small firms all dropped.

Ontario was a bit different. Small firms increased their share of total firms, by a similarly small amount, to 97.9% in 1986, but the distribution was broader. The rate of growth in the number of firms was uniformly between 32% and 35% for all the categories of small business, so that the larger small firms all maintained their share of the total number of firms. This again demonstrates the strength of the maturing small businesses in Ontario and the heavy reliance elsewhere in Canada on start-ups with fewer than five employees.

As Table 7.4 shows, the effect of such a rapid increase in the number of small firms is inevitably to reduce the average number of employees per firm in the whole economy.

Table 7.4
The Downsizing Effect

Average number of employees per firm, by firm size, Canada, 1978 and 1986

	Average employees per firm in Canada	
Firm size	**1978**	**1986**
Fewer than 5	1.4	1.3
5 to 19	9.3	8.8
20-49	29.8	28.8
50-99	67.6	66.1
100-499	197.4	192.5
More than 500	2,428.7	2,396.2
Total	15.2	12.7

These trends become still more clear when the distinction is made between the public and private sectors. In analyzing the private and public sectors, it is more meaningful to group public administration with community services, which include education, health and welfare and religion. Some of these services are provided in a market environment, in competition with other firms, but almost all of them are funded by governments and therefore not subject to direct market forces. These organizations are called the funded sector, and the balance are called the market sector.

For all sizes of firms in Canada, the average number of employees in the market sector fell from 12.8 to 10.4 (down by 19%). In the funded sector, the average fell from 39.0 to 34.8

(down 11%). In Ontario, however, the drops in average size were more moderate. In the market sector, the average fell from 14.7 to 13.0 (down 12%), while organizations in the funded sector didn't change between 1978 and 1986, sticking at 35. In the rest of Canada, excluding Ontario, the average organization size in the funded sector fell 16% from 41.2 to 34.6.

It is possible that the funded sector is more sensitive to the market sector outside Ontario and Quebec, because the other eight provincial economies rely on fewer industries for their industrial base. When those industries are weak, the funded sector tends to follow suit and pull in its belt. In Ontario and Quebec, on the other hand, the provincial governments feel more able to act as countercyclical employers. The downsizing push has also been given an added impetus in the three most westerly provinces, which have been more aggressive in privatizing their crown agencies than the central and eastern provinces.

As for the market sector, the real strength of Ontario lies in its wide range of firms employing 500 to 1,500 people. These firms are more resilient than the very large firms, which are liable to make large cuts in employment when times are difficult (which includes being taken over).

Table 7.5 demonstrates the differences between the market and funded sectors in Canada. Naturally, small firms are much less important in the funded than the market sector. Only 14% of the funded-sector employees are in small firms, compared to 44% in the market sector. And small firms account for only a third of the new jobs in the funded sector, while they account for 107% in the market sector — firms employing more than 500 people lost the equivalent of 10% of all the new jobs created during 1978 to 1987. The resulting shift in the distribution of the labour force by size of firm has raised the share of small firms in the market sector to 44% — which is significantly more than the 40% share of firms employing more than 500 people. This is an exact reversal of the situation in 1978.

The trends are similar in Ontario, although, as always, the large firms are a greater presence. Small firms in the market sector in Ontario are still outnumbered by the firms employing more than 500 people — 39% to 44%, which is

Table 7.5
The Difference Between the Market and Funded Sectors, Canada

Distribution of employment in 1978 and 1986, and of the job gains during 1979-87, by firm size, for the market and funded sectors

Size of firm (employees)	1978 employment distribution for		1979-87 shares of job gains in		1986 employment distribution for	
	Market %	Funded %	Market %	Funded %	Market %	Funded %
Fewer than 20	21.5	5.7	93.6	26.5	24.2	7.2
20 - 99	18.3	6.6	13.2	8.9	19.6	6.4
Small firms	**39.8**	**12.3**	**106.8**	**35.4**	**43.8**	**13.6**
100 - 499	16.1	14.4	4.0	15.6	16.2	13.1
500 or more	44.1	73.3	-10.8	49.0	40.0	73.3
All firms	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

close to the situation that existed for Canada in 1978. This means that in the rest of Canada, small firms account for a much larger portion of total market-sector employment — 47%, compared to 37% for firms employing more than 500 people. With small firms supplying almost half the total jobs in the market sector, the rest of Canada has come to rely on small business to a remarkable degree.

Table 7.6
The Difference Between the Market and Funded Sectors, Ontario

Distribution of employment in 1978 and 1986, and of the job gains during 1979-87, by firm size, for the market and funded sectors

Size of firm (employees)	1978 employment distribution for		1979-87 shares of job gains in		1986 employment distribution for	
	Market %	Funded %	Market %	Funded %	Market %	Funded %
Fewer than 20	18.7	6.2	73.5	19.5	20.1	7.3
20 - 99	16.8	5.9	20.4	5.8	19.0	5.1
Small firms	**35.5**	**12.1**	**93.9**	**25.3**	**39.1**	**12.4**
100 - 499	15.9	10.7	10.3	9.2	17.3	9.1
500 or more	48.6	77.2	-4.2	65.5	43.6	78.5
All firms	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

CHAPTER 8
WINNING AND LOSING INDUSTRIES — AND THE POWER OF SMALL BUSINESS

The shift of the labour force out of goods-producing industries and into services has been progressing for many years now. It started with the mechanization of farm equipment at the beginning of the century, which resulted in the flight of farm workers to the cities. Between 1931 and 1986, the farm population in Canada fell by three quarters[1]. This process has now stabilized, with agricultural employment running at about 4% of the labour force. In 1987, the industry's employment even rose slightly, so it is unlikely it will shift dramatically in the future.

After World War II, the goods-producing industries made something of a comeback. Although the decline of agricultural employment continued, there was a resurgence of goods-producing industries, because construction and manufacturing employment grew strongly as the Canadian economy matured. In the past two decades, however, manufacturing employment has stagnated at around two million (albeit with some sharp cyclical variations), while the labour force has grown by 50%, so manufacturing's share of total employment has dropped significantly. As Chart 8.1 shows, the effect has been to reduce the share of employment of the goods-producing industries dramatically since 1960.

Since 1960, the goods-producing sectors have lost more than 14 percentage points in their share of the total labour force, the biggest part of it going to market services, which have picked up seven points. Governments and their agencies at all levels have also come to play a larger role as employers, picking up more than four percentage points in their share of employment.

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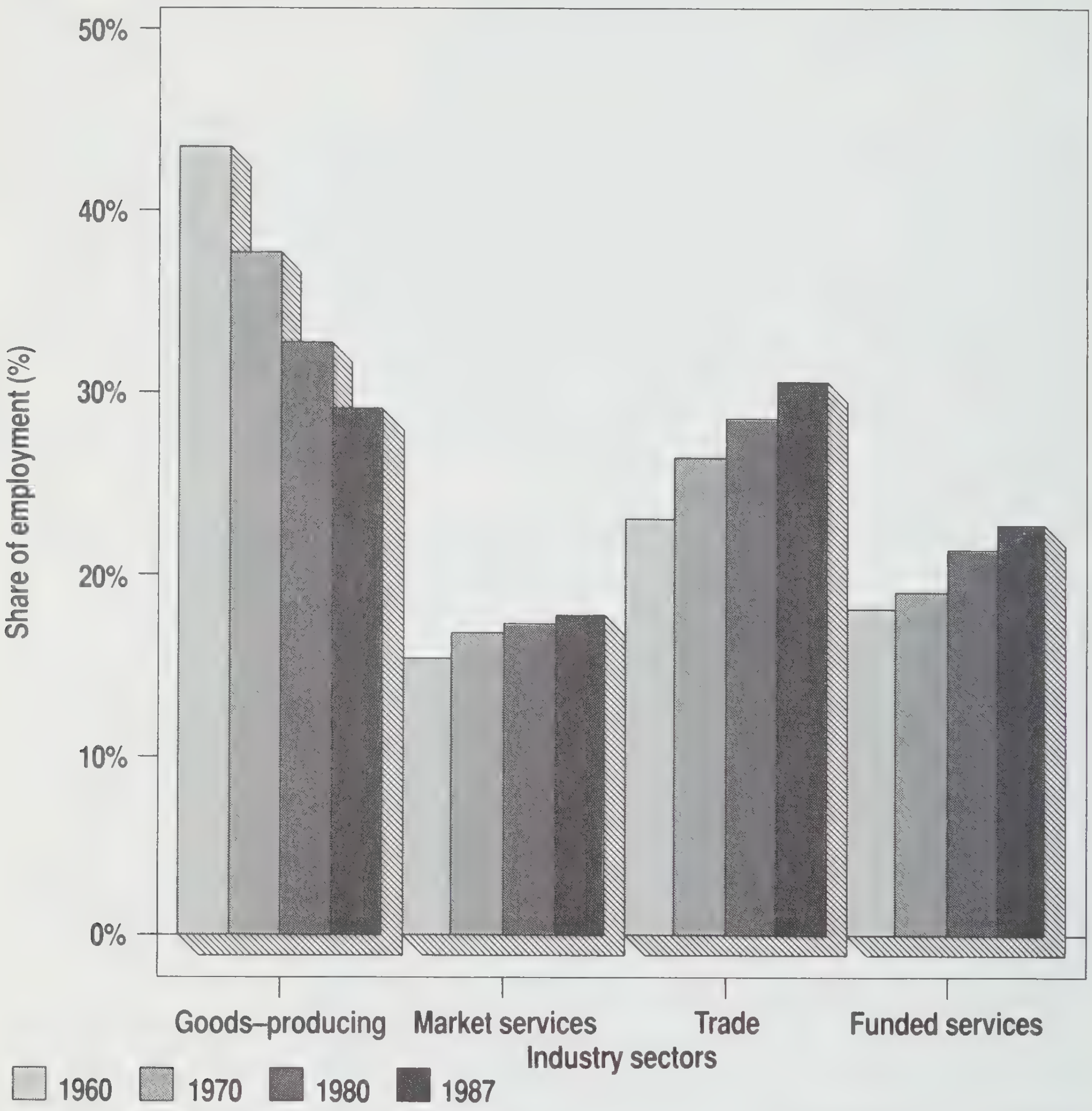
[1] Canadian censuses

Chart 8.1[2]

The Sectors That Are Gaining — and Losing

Share of the Canadian labour force employed in the four major sectors* of the economy in 1960, 1970, 1980 and 1987



* Goods-producing industries include: Primary, Mining, Manufacturing and Construction. Trade includes Retail and Wholesale Trade. Market services include Transportation, Communications & other Utilities, Finance, Insurance and Real Estate and Personal and Business services. Funded services include Public Administration and Community services.

[2] Statistics Canada

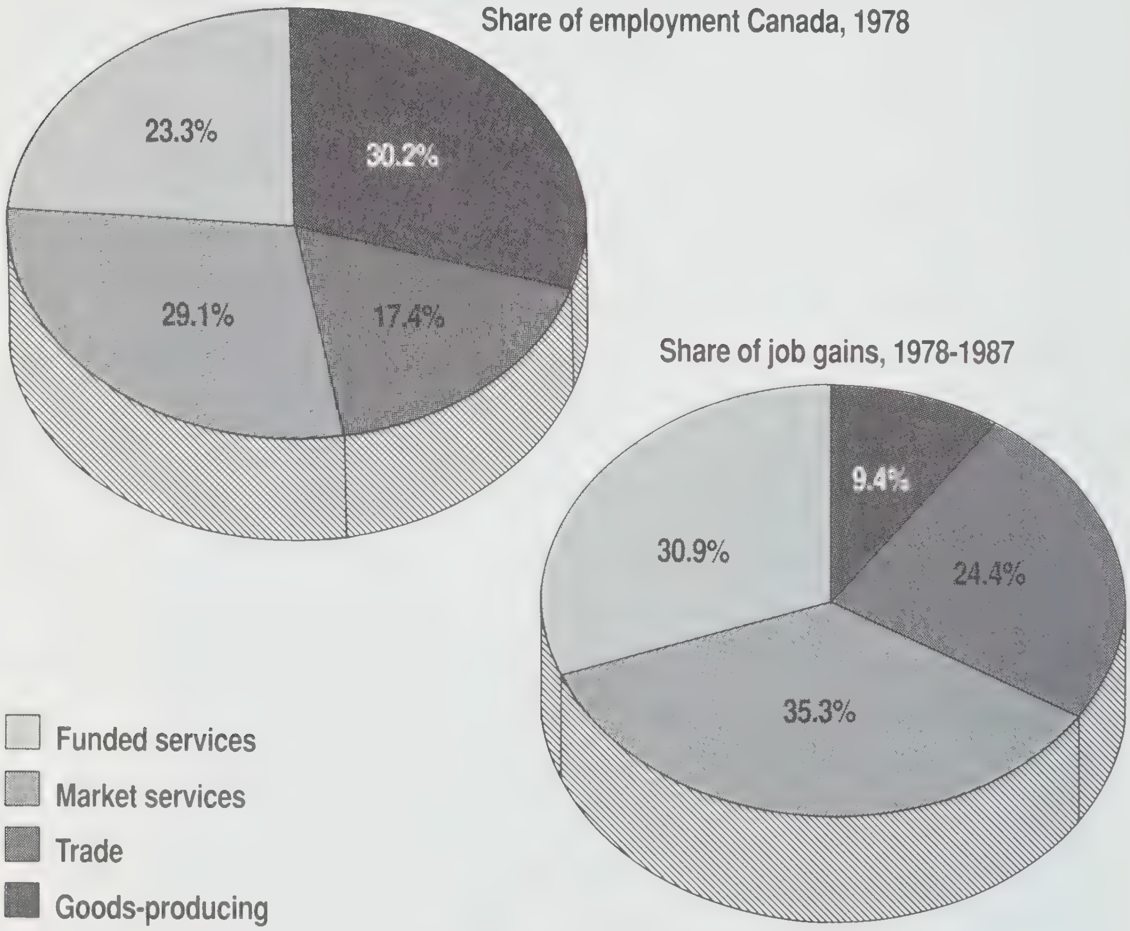
In the nine years to 1987, the process did not run as rapidly as in the previous two decades, with goods-producing industries losing 3.8 percentage points, compared to 5.7 in the 1960s and 5.0 in the 1970s. Nevertheless, the shrinkage continues to be a powerful phenomenon, as the goods-producing industries are winning a very small share of the new jobs created, as Chart 8.2 shows.

The goods-producing industries are generally more sensitive to economic cycles than services. After the most recent recession, which precipitated a drastic cutback in employment during 1982-83, the goods-producing industries reduced their labour force by 14% while the rest of the industries reduced theirs by 4%. Government employment barely changed. In the subsequent boom, the goods-producing industries have grown at close to the same rate as the economy as a whole, including a growth of 3.4% in 1987, when employment in the whole economy grew 3.8%. However, although these industries appear to have stemmed their relative loss of employment during boom times, it remains to be seen if the next recession will once again affect them more than the service side of the economy.

The picture for the goods-producing industries would have been even worse had it not been for Ontario, in which a long construction boom, a prosperous printing and publishing industry and a resurgent auto industry contributed to the goods-producing sector's creating 16% of new jobs, 9% of it from manufacturing. As Table 8.1 shows, however, the rest of Canada didn't do as well. Its goods-producing industries accounted for less than 3% of new jobs, all of them in the primary industries. In absolute terms, the labour force in the four goods-producing industries grew by 162,000 in Ontario during 1978-87, compared to 28,000 in the rest of Canada. Ontario's goods-producing sector now has 30% of its total labour force, compared to the rest of Canada's 24%.

Chart 8.2[3]
Shrinking the Goods-Producing Sector

Share of each sector of total employment in Canada, 1978, and share of new jobs during 1978-87



*See previous chart for a definition of the industry groupings.

[3] Statistics Canada, Business Microdata Integration and Analysis and Small Business and Special Surveys. All data in this chapter are from this source unless otherwise noted.

Table 8.1
Industry Shares of Employment and New Jobs

Distribution, by industry groups, of 1978 employment and of new jobs generated during 1978-87

	Distribution, by industry, of Total employment, 1978			New jobs, 1978-87		
Industry*	Ontario %	Rest of Canada %	All Canada %	Ontario %	Rest of Canada %	All Canada %
Primary	0.7	1.1	0.9	0.8	2.9	1.9
Mining	1.4	2.3	2.0	-0.3	1.7	0.7
Manufacturing	26.9	19.4	22.4	8.6	-3.2	2.7
Construction	4.5	5.2	4.9	6.7	1.3	4.0
T, C & U	9.7	9.4	9.5	-4.6	-3.1	-3.8
Wholesale trade	5.3	5.7	5.6	6.0	4.3	5.1
Retail trade	11.9	11.8	11.8	16.2	21.8	19.0
F, I & RE	6.5	6.0	6.2	9.5	5.6	7.5
Community services	12.8	15.1	14.2	15.6	25.8	20.7
P & B services	13.3	13.3	13.3	28.2	34.1	31.2
Government	6.8	10.4	9.0	12.0	7.8	9.9
Non-classified	0.1	0.3	0.2	1.2	1.0	1.1
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

* The abbreviated industries are: Transportation, Communications and other Utilities; Finance, Insurance and Real Estate; and Personal and Business services. Government includes all three levels of government, but not health & welfare, education and religion, which are included in community services.

Whatever happens to the goods-producing industries, the real job-creating machines are all in services — personal and business services, community services and retail trade. These three pillars of the economy accounted for 39% of total employment in 1978, yet they created 71% of the jobs during 1978-87, as Table 8.1 shows. If Ontario is excluded, the rest of Canada showed an amazing dependence on these three industries, which accounted for 82% of the jobs created during the period.

The three pillars were not quite as dominant in Ontario, where they accounted for 60% of the new jobs on a base of 38% of total employment in 1978. But that is a relative number, which does not reflect the performance of the three pillars in Ontario as much as the stronger overall growth in

Ontario, particularly in the goods-producing sector. As Table 8.2 shows, Ontario's total employment grew by 29% during 1978-87, compared to the rest of Canada's 18%. The three giant job-creators in Ontario all grew at significantly faster rates in Ontario than in the rest of Canada. In the rest of Canada, with its narrower industrial base, however, the three pillars assumed a much greater role than they did in Ontario.

Table 8.2
Small Firms Outgrow Big Firms by a Wide Margin

Employment growth rates, for small firms employing fewer than 100 people and big firms employing more than 100, for Ontario and the rest of Canada, 1978-87

	Employment growth rate, 1978-87, for firms employing					
	fewer than 100		more than 100		all firms	
Industry*	Ontario %	Rest of Canada %	Ontario %	Rest of Canada %	Ontario %	Rest of Canada %
Primary	35.0	57.3	31.6	-16.4	34.7	48.5
Mining	122.9	139.6	-19.5	-12.1	-5.9	13.6
Manufacturing	66.6	35.7	-5.3	-16.3	9.2	-3.0
Construction	65.9	25.8	-5.1	-41.9	43.1	4.6
T, C & U	66.2	37.2	-25.9	-15.7	-13.5	-6.0
Wholesale trade	46.1	21.3	12.3	1.4	32.2	13.6
Retail trade	57.4	49.4	22.8	15.8	38.9	34.0
F, I & RE	89.5	45.1	24.2	4.3	41.6	17.1
Community services	92.4	93.2	24.0	18.2	34.7	31.4
P & B services	80.6	65.4	34.5	17.2	60.4	47.1
Government	37.6	43.7	51.2	12.1	50.5	13.7
Total	**69.3**	**49.7**	**10.3**	**1.4**	**28.6**	**18.4**

* See note to Table 8.1

Ontario experienced much more rapid growth than the rest of Canada in one other area, the funded sector, which grew 50% in Ontario during 1978-87, compared with 14% elsewhere. This growth was almost entirely in the federal civil service, in which employment grew 129%, compared to 11% at the provincial level and 37% at the local level. In the rest of Canada, the civil service grew 17% at the federal level, 7% provincially and 19% locally.

Apart from the funded sector, however, the key to employment growth clearly lies in small firms. The most

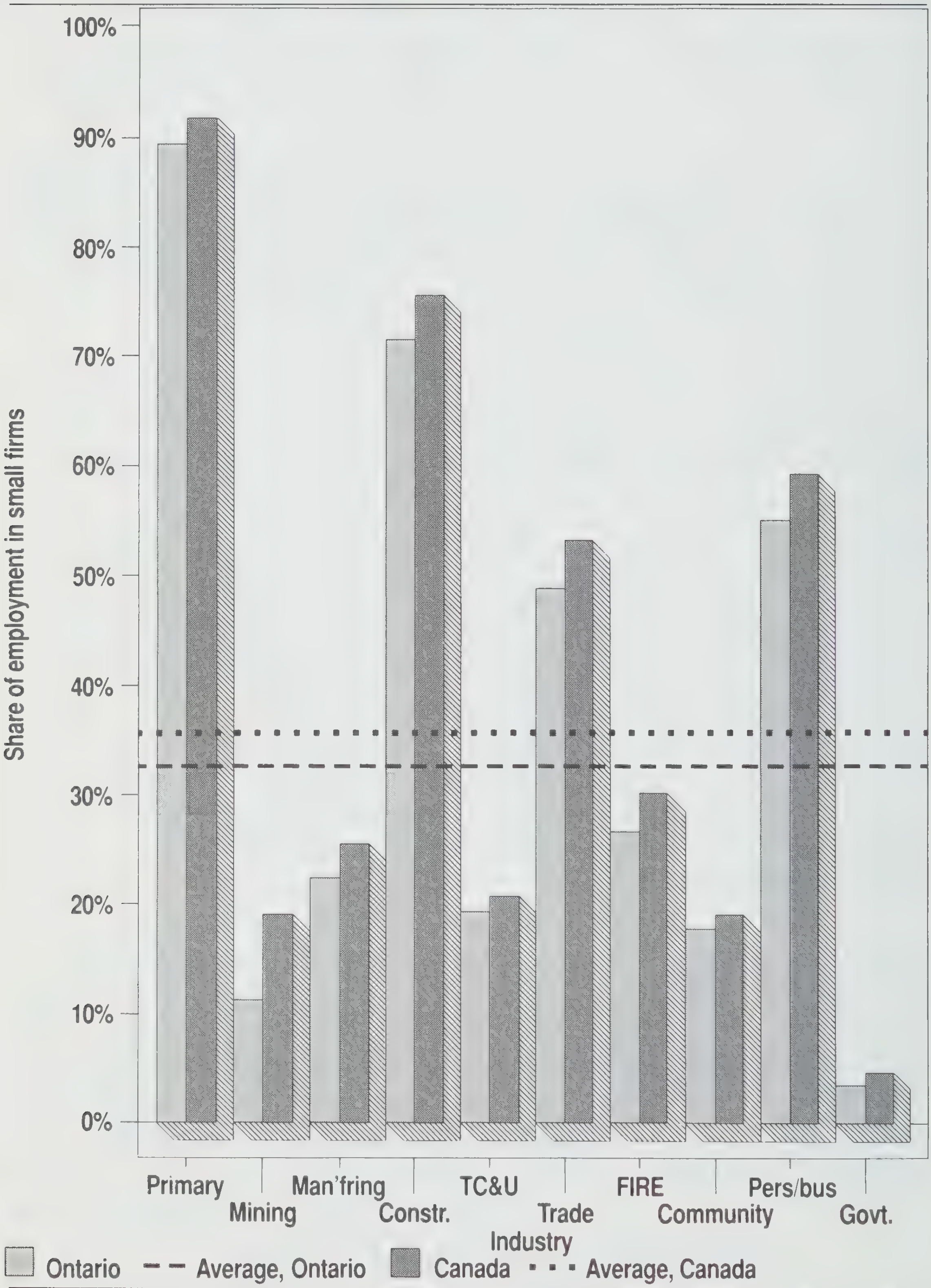
spectacular growth rates came from mining, but employment in mining is such a small part of total employment that the surge of small firms in this sector did not have a major impact. The most remarkable trend is the strong growth in small firms in community services, which is traditionally dominated by large organizations in the health and welfare and educational fields. This was the second fastest growing sector among small firms, and, although less than 20% of 1978 employment in community services was in small firms, the new jobs created by small firms matched those created by the big firms in the industry. Two-thirds of the growth in this industry was in health and welfare, where the explosion of small nursing homes, social services and independent medical centres has fueled a great deal of the job creation.

The real power, however, comes from personal and business services, where firms with fewer than 100 employees grew at 71% during the period in Canada (81% in Ontario and 65% in the rest of Canada). It is reasonable to postulate that these small firms are doing well because of the growth of franchising and because small firms can offer more personalized service than most big firms, so they prosper in service-oriented industries. However, there is no ready explanation why small firms grew so strongly in the goods-producing sector, because it is mostly dominated by big firms, which were cutting back fiercely for most of 1978-87. A priori, one would expect small firms to suffer when big firms retrench. This raises the question of who sets the pace in economic expansions. It would appear to be incorrect to assume that small firms perform well only in industries that are dominated by small firms.

As Chart 8.3 shows, there are really only four industries which can reasonably be described as being dominated by small firms, because they account for more than half the total employment — primary, construction, trade and personal and business services. In all the other industries, big firms employ more than 70% of the labour force. Ontario has a consistently lower proportion of small firms in every industry, but the pattern is the same.

Chart 8.3
The Industries That Small Firms Prefer

Share of total employment in each industry* held by firms with fewer than 100 employees, Ontario and Canada, 1986



* See note to Table 8.1

This is reflected in the employment distribution between industries in small and big firms. As Table 8.3 shows, employment in big firms is heavily concentrated in community services, manufacturing and government, while small-firm employment is heavily concentrated in retail trade and personal and business services. Manufacturing is also strong in small firms, although still way behind the concentration in big businesses.

The patterns in small firms are similar in Ontario and the rest of the country, but in big businesses, Ontario has a much heavier relative weighting in manufacturing and a much lighter one in funded services. Significantly, small firms in manufacturing have an important share of the labour force in Ontario, where manufacturing is doing well, while small manufacturing firms employ a less important share of the labour force in the rest of Canada, where the industry is declining. In the industries that have performed well in both Ontario and the rest of the country, small firms have a comparably important share of the labour force in both.

It appears that a strong small business presence signals a strong economic performance. Chart 8.4 demonstrates the power of this phenomenon for goods-producing industries. As the big-business share of employment rises, employment growth declines. The only industry to buck this trend is mining and even that is a reflection of a spectacular performance by small firms. Mining includes the oil and gas industry, which was the major force behind the 23% growth in the industry in 1979-80, almost all of it from small firms in Alberta. Then the oil and gas industry collapsed and employment in the mining sector declined by 9% between 1981 and 1987. If performance were measured between 1981-87, mining (with its dominant big business presence) would indeed have had the worst performance, with a 12% drop in employment, the worst of the four industries after manufacturing's drop of 2.8%.

The most surprising aspect of this phenomenon is that big firms also tend to perform better when there is a good supply of small firms in their industry. In the goods-producing sector, employment in the big firms declined in all four industries, but their relative performance was tied to the level of small business employment too. Primary had the smallest decline

Table 8.3
Industrial Distribution of Jobs in Small and Big Firms, 1986

The distribution of employment, by industry, for firms employing fewer than 100 people and those employing more than 100

	Distribution of jobs					
	in small firms		in big firms		in all firms	
Industry*	Ontario %	Rest of Canada %	Ontario %	Rest of Canada %	Ontario %	Rest of Canada %
Primary	1.8	3.1	0.1	0.2	0.7	1.3
Mining	0.4	1.3	1.4	2.9	1.0	2.3
Manufacturing	16.6	12.3	27.2	18.2	23.8	15.9
Construction	10.0	9.0	2.0	1.5	4.6	4.4
Goods-producing	***28.8***	***25.7***	***30.7***	***22.8***	***30.1***	***23.9***
Wholesale trade	9.2	8.5	3.4	3.4	5.3	5.4
Retail trade	16.9	19.1	10.2	9.8	12.4	13.3
Trade	***26.1***	***27.6***	***13.6***	***13.2***	***17.7***	***18.7***
T, C & U	4.0	4.4	8.1	9.8	6.8	7.8
F, I & RE	5.6	5.1	7.8	6.3	7.1	5.8
P & B services	26.6	26.2	10.7	9.9	16.2	16.1
Market services	***36.2***	***35.7***	***26.8***	***26.0***	***30.0***	***29.7***
Community services	7.3	8.9	16.9	22.0	13.7	17.0
Government	0.9	1.4	12.0	16.0	8.3	10.4
Funded services	***8.2***	***10.3***	***28.9***	***38.0***	***22.0***	***27.4***
Non classified	0.7	0.7	0.0	0.0	0.2	0.3
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

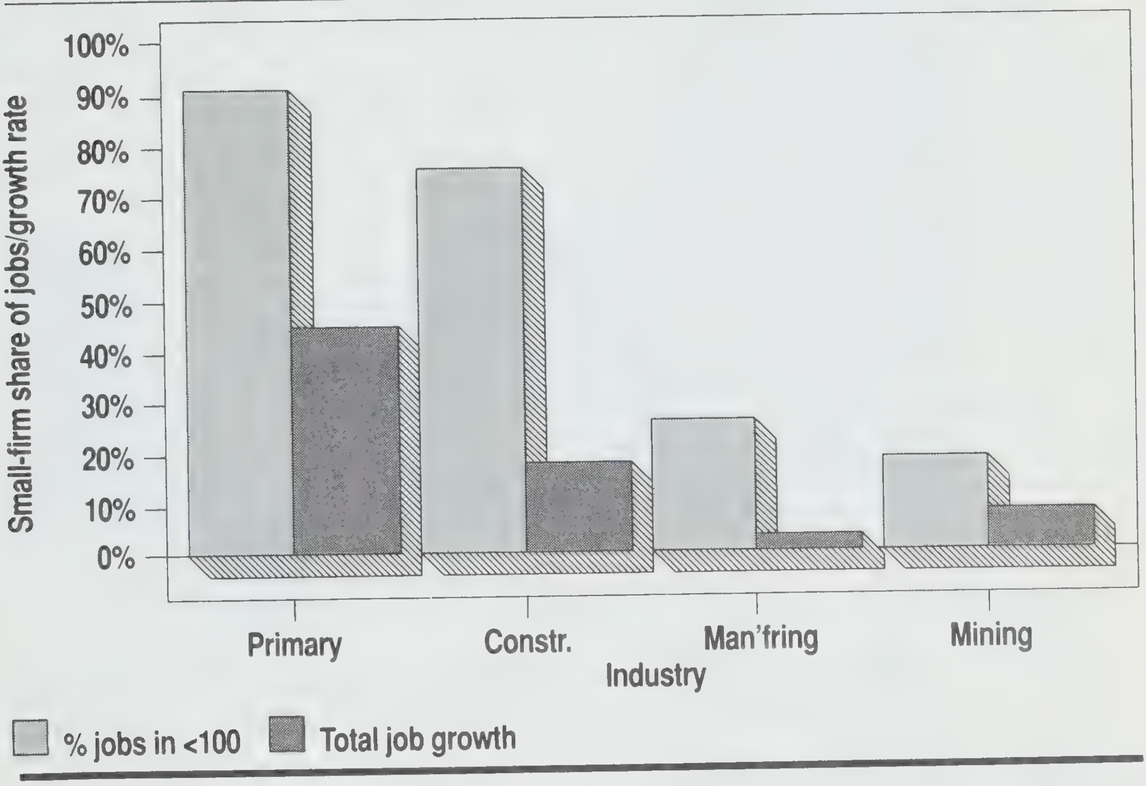
* See note to Table 8.1

in big firms, followed by manufacturing and mines. Only construction bucked the trend, losing 29% of the employment in big firms — and that was largely thanks to changes in the structure of the industry, which shifted toward sub-contracting in non-union companies.

Chart 8.4

Small Firms Attract Growth in the Goods-Producing Sector

Comparison of rate employment growth, 1978-87 and percentage of employment in small firms, 1986, by industry, Canada



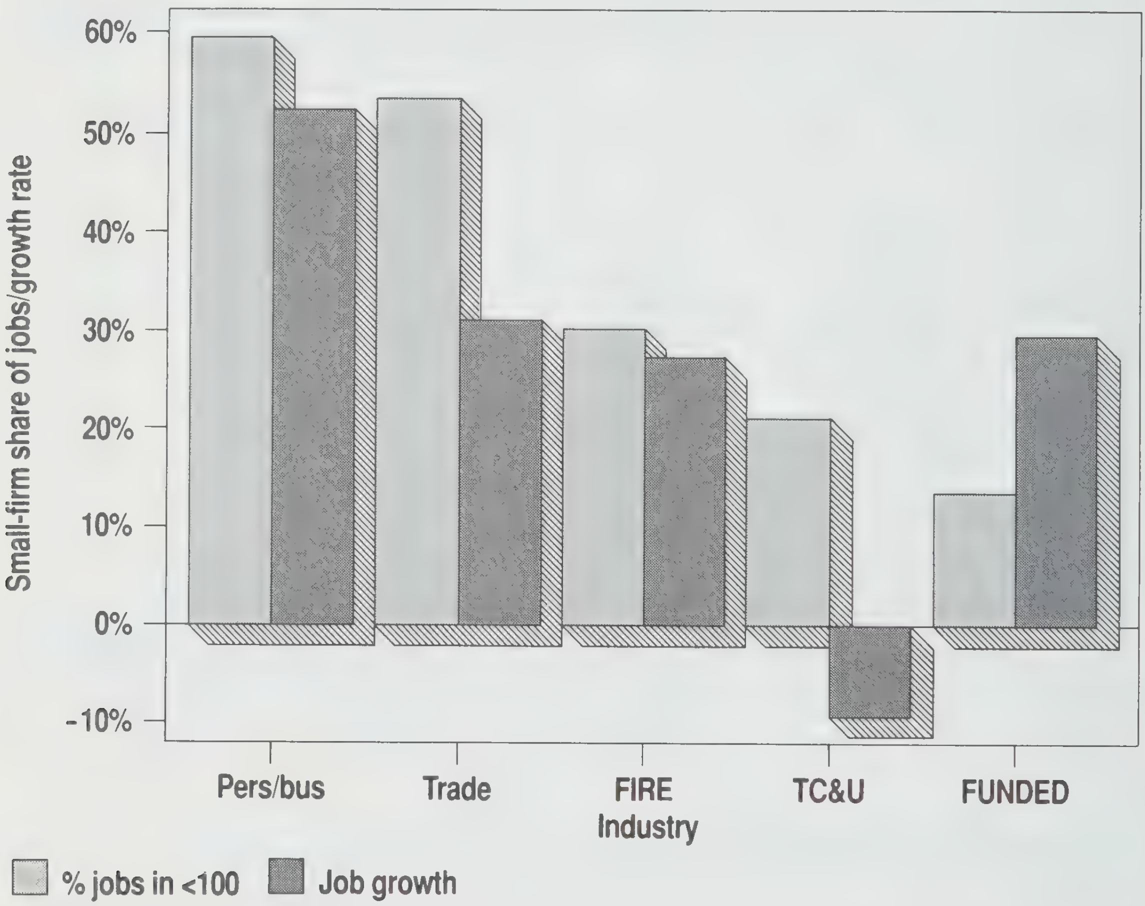
Ontario has a slightly different pattern. Small businesses, of course, represent a smaller share of employment in all industries in Ontario compared to the rest of Canada, particularly in mining, where it is 11.7% in Ontario and 21.2% in the rest of Canada. Ontario also had much stronger growth in construction, which grew fastest among the goods-producing industries, increasing employment by 43% during 1978-87, followed by primary with 35%.

In the service industries, the same phenomenon exists, as Chart 8.5 shows. The higher the small business presence in an industry, the higher its employment growth. Funded

services did not follow this trend, of course, because they must react to forces other than the market.

Chart 8.5
Small Firms Power Employment Growth in Services, Too

Comparison of rate employment growth, 1978-87 and percentage of employment in small firms, 1986, by industry, Canada



Big firms demonstrate the same tendency to perform better in small-business dominated service industries as they do in the goods producing sector. This may be a reflection of the greater resilience of industries with a large base of small firms, particularly in the downsizing of successful big firms, which contract out many services they previously performed in-house. Or it could be an indication that small firms are succeeding most in the healthiest industries. Whatever the reason, a strong small business base appears to help big firms too.

Ontario, once again, is a little different. The trend is still

there, but a strong performance in finance, insurance and real estate made that industry grow at 42%, slightly better than the 37% in trade. Ontario has benefitted from this industry to a far greater degree than the rest of Canada, where employment grew by only 17%, consistent with the trend for growth to follow small business concentrations.

When the contributions of each size category in each industry is analyzed, the importance of the three pillars stands out. As Table 8.4 shows, these industries together account for more than half of all new jobs in firms employing fewer than 100 people. They also account for three-quarters of the growth in mid-sized firms, and more than 90% in the biggest firms. 30% of all new jobs in Ontario during 1978-87 came from firms employing fewer than 20 people in personal business services, community services and retail trade.

The other important contribution came from small firms in manufacturing, which accounted for one-eighth of the total new jobs created. Big manufacturing firms in Ontario lost the equivalent of 4.6% of the new jobs and mid-sized firms made a small contribution to jobs creation.

In the rest of Canada, the imbalances are even more startling. As Table 8.5 shows, half of all the new jobs were created by firms in the three pillars that employ fewer than 20 people. In mid-sized firms, the three industries accounted for 10% of all new jobs, while the other industries combined to lose the equivalent of 5% of new jobs. In the biggest firms, their gains in employment were 12.5% of total gains, while the other industries together lost the equivalent of 12.5% of the total jobs created.

Small firms in personal and business services accounted for almost 30% of total job creation in the rest of Canada. And small firms in manufacturing, despite a small base of only 4.7% of total employment in 1986, contributed an impressive 9.7% of the total gains in employment. Large manufacturing firms, with a base of 11.2% of total employment in 1986, lost the equivalent of 12.8% of the jobs created, leaving manufacturing in all firms in the rest of Canada with a net loss of 3.2% of the jobs created. In the rest of Canada, small firms accounted for 95% of all new jobs. Firms employing fewer than 20 people accounted for 87.5%.

Table 8.4
Where New Jobs Come From, by Industry and Size, Ontario

Percentage contribution to total job creation by each size of each industry, 1978-87

Industry*	Contribution to job creation by firm size					
	0-19	20-99	Small firms	100-499	500 +	Total
	%	%	%	%	%	%
Primary	0.7	0.1	0.8	0.0	0.0	0.8
Mining	0.4	0.1	0.6	0.4	-1.2	-0.3
Manufacturing	9.3	3.3	12.6	0.6	-4.6	8.6
Construction	6.2	0.7	7.0	0.1	-0.3	6.7
Goods-producing	***16.7***	***4.3***	***21.0***	***1.1***	***-6.2***	***15.9***
Wholesale trade	4.6	0.5	5.1	0.6	0.3	6.0
Retail trade	8.8	2.3	11.2	1.8	3.2	16.2
Trade	***13.4***	***2.8***	***16.2***	***2.5***	***3.5***	***22.2***
T, C & U	2.1	0.9	3.0	0.1	-7.8	-4.6
F, I & RE	3.9	1.5	5.4	0.6	3.4	9.5
P & B services	16.2	5.0	21.2	3.2	3.9	28.2
Market services	***22.3***	***7.4***	***29.7***	***3.9***	***-0.4***	***33.1***
Community services	5.0	1.5	6.5	2.3	6.8	15.6
Government	0.4	0.1	0.5	0.3	11.2	12.0
Funded services	***5.4***	***1.6***	***7.0***	***2.5***	***18.1***	***27.6***
Non-classified	0.9	0.3	1.2	0.0	0.0	1.2
Total	**58.6**	**16.4**	**75.0**	**10.0**	**15.0**	**100.0**

*See note to Table 8.1

Table 8.5
Where New Jobs Come From, by Industry and Size, the Rest of Canada

Percentage contribution to total job creation by each size of each industry, 1978-87

Industry*	0-19 %	20-99 %	Small firms %	100-499 %	500 + %	Total %
	Size of firm by number of employees					
Primary	3.3	-0.2	3.0	-0.1	0.0	2.9
Mining	2.0	1.0	3.0	0.0	-1.3	1.7
Manufacturing	10.1	-0.5	9.7	-2.7	-10.1	-3.2
Construction	7.0	-2.0	5.0	-1.3	-2.4	1.3
Goods-producing	***22.4***	***-1.7***	***20.6***	***-4.1***	***-13.8***	***2.7***
Wholesale trade	5.6	-1.5	4.1	-0.7	0.9	4.3
Retail trade	15.3	1.9	17.2	0.6	4.0	21.8
Trade	***20.9***	***0.4***	***21.3***	***-0.1***	***4.9***	***26.1***
T, C & U	3.7	-0.2	3.5	-0.4	-6.2	-3.1
F, I & RE	4.1	0.5	4.6	0.4	0.5	5.6
P & B services	24.9	4.5	29.4	2.2	2.5	34.1
Market services	***32.7***	***4.8***	***37.5***	***2.2***	***-3.1***	***36.6***
Community services	10.0	3.5	13.5	6.5	5.8	25.8
Government	0.9	0.4	1.2	0.5	6.1	7.8
Funded services	***10.8***	***3.9***	***14.7***	***7.0***	***11.9***	***33.6***
Non-classified	0.7	0.2	0.9	0.1	0.0	1.0
Total	**87.5**	**7.4**	**95.0**	**5.0**	**0.0**	**100.0**

*See note to Table 8.1

Manufacturing

The manufacturing industries that have grown fastest in Ontario have been furniture and fixtures, printing and publishing, the wood industries and rubber and plastics, all of which grew more than 27% in the nine years 1978-87. As Table 8.6 shows, the next best industry was transportation equipment (mainly the automobile industry), with 12% growth. However, the auto industry accounts for 15% of all manufacturing employment in Ontario, so its growth rate packs the biggest punch in terms of actual new jobs.

Table 8.6
The Manufacturers that Grew the Most

Distribution of employment in 1986 and growth rates, for small and big firms in manufacturing industries, during 1978-87. Ranked by growth rate.

Industry	Share of 1986 employment %	Employment growth 1978-87 Small firms %	Big firms %	All firms %
Furniture & fixtures	3.6	75.4	14.1	42.9
Printing & publishing	7.8	56.4	20.0	31.8
Wood industries	2.9	63.8	-3.5	30.4
Rubber and plastics	5.4	136.4	0.3	27.2
Transportation equipment	15.3	134.6	5.0	12.4
Clothing	2.9	53.9	-12.9	12.1
Electrical & electronic	8.1	117.5	-0.7	11.7
Non-metallic minerals	2.9	48.3	-1.8	8.4
Food and beverage	10.0	42.9	1.5	8.0
Leather	1.1	13.8	2.4	5.3
Metal fabricating	9.4	51.1	-28.0	3.0
Chemicals	6.1	70.4	-7.3	1.4
Paper & allied	5.0	87.5	-8.5	0.4
Machinery	5.1	62.8	-23.1	0.4
Textiles	2.3	50.0	-13.2	-0.4
Knitting mills	0.7	52.6	-21.7	-3.8
Petroleum & coal	0.8	200.0	-12.8	-8.3
Primary metal	5.5	51.4	-19.6	-15.8
Tobacco products	0.2	-50.0	-38.2	-38.9
Miscellaneous	4.7	63.6	-12.1	14.3
Total	**100.0**	**66.4**	**-5.3**	**9.1**

The industries that were least successful during the period were tobacco products and primary metals, which reduced their employment by 40% and 16% respectively. Apart from these two, however, there were few dramatic job losses in any manufacturing industry.

As noted before, big firms reduced their labour force in practically all manufacturing industries. The only industries to show strength in the big firms were transportation equipment and printing and publishing, which include, of course, the province's booming auto industry and the prosperous media industry.

However, almost all industries grew strongly in the small-firm sector. Employment in small firms grew by more than 50% during 1978-87 (or 5% a year on average) in all but four of the manufacturing industries, as Table 8.6 shows. Small business growth was particularly strong in transportation equipment, rubber and plastics and the electrical and electronic industries. These three industries were among the top four contributors to overall employment growth in manufacturing, as Table 8.7 shows.

When these growth rates are translated into new jobs, the weight of the industries with the biggest workforces lends their growth rates more importance. Printing and publishing

Table 8.7
The Manufacturing Firms that Made a Difference

Contribution to total gain in manufacturing employment, by size of firm and industry, 1978-87. Grouped by biggest and smallest employers and ranked by contribution to employment increase

Industry	Share of total employment gains by firm size					
	0-19 %	20-99 %	All small firms %	100-499 %	500 + %	Total %
Printing & publishing	11.6	1.4	12.9	1.8	7.8	22.6
Transportation equipment	6.9	5.4	12.4	7.8	-0.1	20.1
Rubber & plastics	8.4	5.2	13.6	2.5	-2.4	13.7
Electrical & electronic	6.2	4.4	10.7	1.2	-1.8	10.1
Food & beverage	5.1	2.4	7.5	1.5	-0.1	8.9
Metal fabricating	18.7	3.2	21.9	-6.2	-12.4	3.3
Chemicals	3.3	2.4	5.7	2.2	-6.8	1.0
Paper & allied	2.4	2.4	4.8	-0.1	-4.4	0.2
Machinery	8.4	1.9	10.3	-1.2	-8.9	0.2
Primary metal	1.2	0.9	2.2	-1.0	-13.5	-12.4
Ten Biggest Employers	***72.2***	***29.6***	***101.8***	***8.5***	***-42.6***	***67.7***
Furniture & fixtures	9.0	1.8	10.8	4.9	-2.6	13.1
Wood industries	5.7	2.7	8.4	-0.3	-0.1	7.9
Other 8 industries	21.2	4.0	25.2	-5.9	-8.0	11.3
Ten Smallest Employers	***35.9***	***8.5***	***44.4***	***-1.3***	***-10.7***	***32.3***
Grand Total	**108.1**	**38.1**	**146.2**	**7.2**	**-53.3**	**100.0**

(which accounts for 3.6% of manufacturing employment) had to grow 31% to become the biggest single job creator, just beating out the transportation industry with its 12% growth rate on a base of 15.3% of manufacturing employment.

One half of all new jobs in manufacturing came from small firms in just four industries — printing and publishing, transportation equipment, rubber and plastics and electrical and electronic. The most spectacular performance came from small metal-fabricating firms, which accounted for a fifth of all new jobs in manufacturing in the province.

Services

The star performer in services is the industry that serves the needs of business. This industry has raised its share of employment in services from 17% in 1978 to 21% in 1986, thanks to its generating almost 30% of all the new jobs in services. As Table 8.8 shows, it comfortably outpaces the next best industry, health and welfare, which accounted for 23% of employment growth. Employment in services is now dominated by four industries that each account for about one fifth of total employment — education, health and welfare, services to business and food and beverage. This is a quite different situation from 1978, when education had one-quarter of service employment and services to business only 17%.

Services to business and health and welfare have been the powerhouses behind the strength of personal and business services and community services, respectively. These two are also the industries which had the strongest small business growth, as Table 8.9 shows. This is no surprise in services to business, in which small firms provide a little less than a half of total employment and where small firms have long shown that they can compete effectively. But it is a surprise in health and welfare, which has traditionally been dominated by big organizations. Despite having an employment base only one-third that of big firms, the small firms in this industry generated exactly the same number of new jobs as big organizations during 1978-87. This was achieved by a growth of more than 100% in small firms, or an average of 8% a year.

Small firms in services to business grew even faster, at 125% over the nine years, or 9.4% a year. Services to business also had the strongest growth in big firms, however, which

Table 8.8
The Changing Weights in Service Industries

The distribution, by industry, of employment in 1978 and 1986, and of the increase in jobs between 1978 and 1987, Ontario

Industry	Employment 1978 %	Industry share in: Increase in employment 1978-87 %	Employment 1986 %
Education	25.7	11.4	21.1
Health & Welfare	22.3	23.2	22.6
Cultural	1.0	0.9	1.0
Amusement & recreation	3.8	2.7	3.5
Services to business	17.1	29.8	21.2
Personal services	3.5	4.1	3.7
Accommodation & food	21.2	16.8	19.8
Miscellaneous	5.3	11.2	7.2
Total	**100.0**	**100.0**	**100.0**

helped it to grow 83% over the nine years, by far the fastest growth of any industry in any group. Although personal services has only 3.7% of employment in services, it had the second fastest growth, at 55%, and is likely to show strong growth in coming years.

Table 8.9
Small-Business Power in Service Industries

Employment growth rates, by industry, in firms employing fewer than 100 and more than 100, 1978-87, Ontario

Industry	Employment growth, in small firms %	big firms %	all firms %
Education	93.0	17.6	21.2
Health & welfare	100.8	33.1	49.9
Cultural	41.9	40.0	41.7
Amusement & recreation	43.6	15.9	33.4
Services to business	125.5	45.8	83.3
Personal services	61.2	36.3	55.2
Accommodation & food	54.9	14.9	37.9
Miscellaneous	109.5	84.2	100.2
Total	**83.1**	**27.7**	**47.8**

Average Salaries

The new jobs may all be coming in the small firms, but, as yet, the big salaries are not. As Table 8.10 shows, the smaller firms pay their employees a significantly lower salary than the bigger firms. This appears to be particularly so for firms employing fewer than five people, but this is probably an exaggeration. The low average salary in these very small firms, many of which are start-ups, is probably more a reflection of the greater reliance on part-time workers than on full-time salaries. Even for the larger small firms, however, there is still a large gap between wages paid in big firms and small firms. The only exception is trade where salaries are lower for firms employing more than 500 people than they are for firms employing 20 to 499.

Table 8.10[4]

How Salaries Compare in Different Sized Firms

Payroll divided by individual labour units, by industry category and firm size, Ontario, 1986

Sector	Average salary All firms $	Average salaries for firms employing: 0-4 $	5-19 $	20-49 $	50-99 $	100-499 $	500+ $
Goods producing	22,613	9,616	15,898	19,370	21,119	23,195	28,921
Trade	15,306	9,271	14,468	17,577	19,749	19,464	15,015
Market services	17,869	10,285	12,571	13,690	15,378	18,556	23,854
Funded services	22,181	11,082	12,573	13,411	14,348	18,549	24,573
All Sectors	**19,823**	**9,865**	**14,033**	**16,463**	**18,286**	**20,620**	**24,475**

The effect of these variances on the distribution of payroll between the different firm sizes is notable. As Table 8.11 shows, firms employing more than 500 people account for 57% of the total payroll in Ontario, compared to their 46% share of employment[5]. Small firms account for 28% of payroll, compared to 39% of full-time and part-time jobs. The greatest variances are in the goods-producing and funded services

[4] Statistics Canada, *Business Microdata Integration and Analysis and Small Business and Special Surveys*. Special run for individual labour units and payroll.

[5] Note that the shares of employment in these tables differs from the statistics used previously. Those used in the rest of this report count part-time employees as fractions of full-time jobs. The statistics used in the tables in this section count part-time workers as "individual labour units".

sectors, indicating this is where most of the part-time jobs are found. In trade, the shares of small firms in total employment and payroll are quite close.

Table 8.11
Distribution of Total Payroll by Size Within Category

Share of total payroll of each size of firm within each category Ontario, 1986

Sector	Total payroll All firms $ million	Distribution, by firm size within categories, of payroll 0-99 %	100-499 %	500+ %	of employment 0-99 %	100-499 %	500+ %
Goods producing	36,507	28.4	19.1	52.3	40.1	18.6	40.9
Trade	13,628	52.2	16.8	30.9	55.2	13.3	31.5
Market services	26,645	33.3	14.2	52.5	47.0	13.7	39.3
Funded services	25,067	8.6	7.9	83.2	15.1	9.4	75.1
Unclassified	293	96.4	3.6	0.0	98.9	1.1	0.0
All Sectors	102,140	28.2	14.7	57.0	39.5	14.2	46.1

It is notable, however, that the wage gap is much smaller in services than in the goods-producing sector or in trade. This has an interesting effect when the distribution of total payroll is analyzed by size. As Table 8.12 shows, manufacturing payrolls average more than 40% of the total payrolls for firms with 20-499 employees, compared to about 30% in the smallest firms. And services average about a third of the total payrolls of firms with fewer than 20 employees, compared to about a quarter for the rest.

Table 8.12
Distribution of Total Payroll by Industry and Size

Share of total payroll within each size group, by industry sector, Ontario, 1986

Sector	Sector share of total payroll for firms employing: All firms %	0-4 %	5-19 %	20-49 %	50-99 %	100-499 %	500+ %
Goods producing	35.7	30.6	32.4	38.7	42.8	46.3	32.8
Trade	13.3	22.1	28.0	25.3	21.6	15.3	7.2
Market services	26.1	34.6	31.9	29.5	27.2	25.2	24.0
Funded services	24.5	10.5	6.7	5.9	7.9	13.1	35.9
All Sectors	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Distribution of Jobs and Firms in Ontario

The tables on the following pages show the distribution, by industry and size, of Ontario firms (Table 8.13) and of employment in Ontario (Table 8.14).

Table 8.13
Distribution of Ontario Firms, by Industry and Size, 1986

Industry	Percentage of firms that are: Small firms	Medium firms	Large firms	Number of firms	Share of total
Primary	99.9	0.1	0.0	18,254	6.2
Mining	88.7	6.8	4.5	903	0.3
Manufacturing	91.2	6.6	2.2	22,705	7.7
Food and beverage	89.8	6.4	3.8	1,924	
Tobacco products	50.0	10.0	40.0	10	
Rubber and plastics	86.2	9.6	4.2	879	
Leather	81.1	16.7	2.2	227	
Textiles	87.1	10.0	2.9	630	
Knitting mills	75.6	23.5	2.9	136	
Clothing	90.1	8.5	1.4	916	
Wood industries	95.6	5.3	1.1	1,288	
Furniture & fixtures	95.7	3.7	0.6	1,756	
Paper & allied	79.2	11.8	9.0	434	
Printing & publishing	95.5	3.5	1.0	3,169	
Primary metal	78.4	14.2	7.4	282	
Metal fabricating	94.3	4.8	0.9	3,988	
Machinery	91.1	6.9	2.0	1,474	
Transportation equipment	81.3	13.1	5.6	869	
Electrical & electronic	87.0	8.8	4.6	959	
Non-metallic minerals	92.1	5.6	2.3	645	
Petroleum & coal	82.3	5.9	11.8	51	
Chemicals	81.7	13.0	5.3	792	
Miscellaneous manuf'rg	94.5	4.8	0.7	2,276	

Table 8.13 (continued)
Distribution of Ontario Firms, by Industry and Size, 1986

Industry	Percentage of firms that are: Small firms	Medium firms	Large firms	Number of firms	Share of total
Construction	99.2	0.7	0.1	36,001	12.2
T, C & U	96.5	2.5	1.0	10,440	3.5
Wholesale trade	97.2	2.4	0.4	19,328	6.6
Retail trade	98.9	0.9	0.2	46,833	15.9
F, I & RE	98.1	1.4	0.5	20,490	7.0
Services	98.4	1.2	0.4	107,047	36.4
Education	88.7	4.8	6.5	2,211	
Health & welfare	97.5	1.7	0.8	18,096	
Cultural	99.8	0.2	0.0	5,920	
Amusement & recreation	98.6	1.2	0.2	5,183	
Services to business	98.1	1.5	0.4	26,037	
Personal services	99.8	0.2	0.0	20,347	
Accommodation & food	98.4	1.3	0.3	18,885	
Miscellaneous services	98.6	1.1	0.3	10,368	
Government	87.9	6.8	5.3	1,144	0.4
Non-classified	99.9	0.1	0.0	7,115	2.4
Total - All industries	**98.9**	**1.6**	**0.5**	**290,260**	**100.0**

Table 8.14
Distribution of Ontario Employment, by Industry and Size, 1986

Industry	Percentage of employment in: Small firms	Medium firms	Large firms	Total employment	Share of total
Primary	89.4	8.9	1.7	30.2	0.7
Mining	11.7	12.1	76.2	45.3	1.0
Manufacturing	23.3	21.9	54.8	1,040.7	23.8
Food and beverage	16.7	17.1	66.2	100.6	
Tobacco products	3.8	7.7	88.5	2.6	
Rubber and plastics	20.8	24.5	54.7	54.8	
Leather	20.3	36.7	43.0	12.8	
Textiles	27.2	38.1	34.7	23.9	
Knitting mills	26.0	60.3	13.7	7.3	
Clothing	44.4	35.6	20.0	29.2	
Wood industries	50.2	36.1	13.7	27.7	
Furniture & fixtures	45.3	28.2	26.5	36.2	
Paper & allied	12.1	13.3	74.6	52.0	
Printing & publishing	32.2	20.2	47.6	79.4	
Primary metal	6.3	14.2	79.5	59.1	
Metal fabricating	36.5	27.7	25.8	108.0	
Machinery	34.4	28.7	36.9	53.6	
Transportation equipment	6.0	14.6	79.4	157.9	
Electrical & electronic	13.4	14.8	71.8	82.5	
Non-metallic minerals	23.1	17.0	59.9	29.4	
Petroleum & coal	4.9	2.0	93.1	10.2	
Chemicals	13.3	24.8	61.9	63.7	
Miscellaneous manuf'rg	38.8	30.6	30.6	49.7	

Table 8.14 (continued)
Distribution of Ontario Employment, by Industry and Size, 1986

Industry	Percentage of employment in: Small firms	Medium firms	Large firms	Total employ-ment	Share of total
Construction	71.5	18.6	9.9	202.8	4.6
T, C & U	19.5	13.3	67.2	295.8	6.8
Wholesale trade	57.2	24.1	18.7	233.1	5.3
Retail trade	45.3	11.1	43.6	543.1	12.4
F, I & RE	26.5	13.1	60.4	310.1	7.1
Services	37.9	14.8	47.3	1,306.0	29.8
Education	4.3	6.3	89.4	290.8	
Health & welfare	27.9	18.0	54.1	297.8	
Cultural	84.6	10.0	5.4	13.0	
Amusement & recreation	60.4	19.6	20.0	47.5	
Services to business	45.6	21.3	33.1	251.0	
Personal services	75.6	11.4	13.0	49.3	
Accommodation & food	59.0	13.6	27.4	268.9	
Miscellaneous services	55.2	18.0	26.8	87.7	
Government	3.6	4.1	92.4	364.2	8.3
Non-classified	97.1	2.9	0.0	10.2	0.2
Total - All industries	**33.2**	**15.5**	**51.2**	**4,381.6**	**100.0**

CHAPTER 9
THE DYNAMICS OF BUSINESS AND EMPLOYMENT

Small businesses, as a group, can reasonably lay claim to being the most dynamic part of the economy, as they consistently provide the lion's share of new jobs. But individually, they often lead a precarious existence. The turnover of businesses is staggering. Although each one is different, small firms seem to follow four basic patterns of behaviour as they start, grow, decline or fail:

- A relatively small proportion are major success stories, including a handful of super performers who account for a wildly disproportionate share of the total employment gains;
- A lot more are as ambitious as the first category, with dreams just as grand, but they fail, for a myriad of reasons, some of which are their own fault, some of which are not. Many of these people learn from their experience and go on to succeed in subsequent business ventures;
- In between, there is a large number of small business owners — about 40% of all business owners — who earn a comfortable living, but have no desire for more than marginal growth; and
- Finally, there are the small businesses that survive but never acquire any momentum, growing in good times and shrinking in bad times, flirting constantly with disaster, sometimes for many years.

It makes for a volatile mix, with businesses starting, failing, merging, selling out, growing and declining in astonishing volumes. Table 9.1 shows how this churning affects the size categories that have been used in all the analysis in this section of The State of Small Business. It's obvious the firms in these categories are a moving target, to say the least. Almost half the 1978 firms ceased operations, but they were replaced one and a half times by new ventures. The most unexpected result of this analysis, however, is the

degree of movement between size categories by firms that are growing (growers) and declining (sliders). In each category other than the smallest, the inflowing firms that had grown or slid out of other size categories represented more than half the total number of firms in that category in 1978.

Most of this inflow is smaller firms growing into bigger categories. Table 9.1 shows just how strong Ontario's corporations are in the critical categories where employment per firm is 50 to 500. This has traditionally been the weakest sector of the Canadian economy, but not in Ontario, where inter-category transfers increased the three biggest size categories by 87%, 58% and 52% respectively. The larger small firms, employing 50 to 99 people were the strongest sector of all, which augurs well for future job creation in the province.

In the rest of Canada, the flow into these categories ran far slower, at about 40% Ontario's rate in firms employing 50 to 99 people and at about 20% of Ontario's rate in firms employing 100 to 499 people. In the largest firms, there was a net loss of about 10% of the firms from transfers between categories.

Looking at this churning from the other end of the telescope — the source category of the moving firms — Table 9.1 shows that a third or more of the 1978 firms employing 5 to 99 people either grew out of their category or declined into lower ones. In firms employing 50 to 99 people, a total of 91% of the 1978 firms (including a good portion of the entrants during the period) grew or declined into other categories. The category wasn't depleted, however, because these firms were replaced by an inflow of 117%, most of which was smaller firms growing into this category. Only a third of the 1978 firms in this category were still there in 1985.

In the smallest firms, employing fewer than five people, all the power comes from start-ups, as is well known. Because of the huge numbers of firms in this category (72% of all firms), bigger firms declining into the category do not make much of a dent, but new ventures added 87% more firms during the seven year period. This is comfortably ahead of the 50% lost to failures. An impressive 11% of the firms in this category grew into bigger categories.

It is surprising just how much turnover there was in the largest firms, which employ more than 500 people. These

Table 9.1[1]
The Volatility of Small Businesses

Turnover in each size category during 1978-85 — from new firms, exits, and growth or decline into other size categories — expressed as a percentage of the number of firms in 1978, Ontario

Type of change	Percentage change by size of firm (number of employees) <5 %	5-<20 %	20-<50 %	50-<100 %	100-<500 %	500+ %	Total %
Base, 1978	**100**	**100**	**100**	**100**	**100**	**100**	**100**
Firms coming into the size category:							
Entrants	87	45	33	30	23	17	74
Inflow*	5	45	67	87	58	52	18
Total	92	90	100	117	81	69	92
Firms leaving the size category:							
Exits	50	33	31	32	33	30	46
Growers*	11	16	27	42	15	0	13
Sliders*	0	16	19	17	11	8	4
Total	**61**	**65**	**77**	**91**	**59**	**38**	**63**
Net change in category	**+31**	**+25**	**+23**	**+26**	**+22**	**+31**	**+29**

* Note: Growers are the firms that have grown enough to graduate to the size category above them (or, sometimes one or two categories beyond that). Sliders decline to a lower category. Inflow is the other side of the coin — additions to a size category by firms that were in a smaller category and grew into it, or by firms that were in a bigger size category and declined into it.

firms, fewer than 1,500, lost almost 40% of their number to failures and downsizing, but still managed to increase their total number by 31%. This was due mainly to the mid-sized firms that grew into large firms, but births also played an important role. A surge of almost 600 firms that graduated into the biggest size category and another 200 that started up big-time new ventures employing more than 500 employees together swelled the ranks of big businesses by more than two-thirds of all big firms operating in 1978.

[1] Source: The statistics in this chapter are based on *Increasing and Declining Employment in Continuous Companies, by Province, Canada, 1978-1985*, Statistics Canada, 1987. This is a special run of the data contained in *Employment Dynamics by Province, Industry Classification, Firm Size and Life Status, 1978-1985.*

Growth and Decline in the Job Market

The impact of this turnover becomes even more dramatic when jobs are added to the equation. As Table 9.2 shows, the major contribution to job creation came from new ventures. The firms that existed in 1978 employed 4% fewer people in 1985, but new ventures added 74% to the number of firms and created 104% of the total new jobs generated over the period. However, the most spectacular contribution came from the handful of firms — a mere 8% of the total number of firms — that grew into a bigger size category. They created 64% of all the new jobs during 1978-85.

Table 9.2
The Big Hitters and the Big Losers

Distribution of firms by status and the corresponding net gains and losses of employment, 1978-85, Ontario

	Firms in each status		Net employment gains/losses	
Status	Number	As a % of 1978 firms %	Number (000s)	As a % of total gains %
Exits	98,096	46	-470.3	-74
Unchanged	90,946	42	209.7	33
Growers	16,808	8	406.5	64
Sliders	9,687	4	-173.0	-27
1978 firms	**215,537**	**100**	**-522.4**	**-4**
Entrants	160,089	74	666.3	104
Net change*	**61,993**	**28**	**1,306.8**	**100**

* Net change in firms is entrants less exits.
Note: Growers are the firms that have grown enough to graduate to the size category above them (or, sometimes one or two categories beyond that). Sliders decline to a lower category.

The job losses from firms that shrank into smaller size categories were also not insignificant — although these firms were only 4% of the firms that existed in 1978, the jobs lost from their downsizing subtracted 27% of the total net gain in employment during 1978-85. By contrast, the 42% of firms that remained in the same size category throughout 1978-85 developed at a more stately pace, accounting for 33% of the total increase in jobs.

Overall, the firms that were operating in 1978 had almost exactly the same number of employees in 1985 as they did in 1978. However, this "stagnation" hid a major loss of almost half of all the 1978 firms, that, between them, lost three quarters of all the new jobs created by start-ups during the seven year period. To put it another way, for every two jobs created by start-ups and expansions, one was lost to failures and downsizing.

Table 9.3 takes this a step further, breaking down the job creation statistics by size of firm in 1978.

Table 9.3
New Jobs and Firms in Transition

Share of total gains in employment in Ontario during 1978-85, by firm size and status

	Size of firm (by number of employees) %						
Status	**<5**	**5-<20**	**20-<50**	**50-<100**	**100-<500**	**500+**	**Total**
Exits	-13	-17	-12	-8	-14	-9	-74
Unchanged	2	2	1	1	6	21	33
Growers	15	15	11	9	13	0	64
Sliders	0	-5	-5	-4	-6	-7	-27
1978 firms	**4**	**-5**	**-5**	**-2**	**-1**	**5**	**-4**
Entrants	39	25	13	8	11	9	104
Total	**43**	**20**	**8**	**6**	**10**	**14**	**100**

Note: Growers are the firms that have grown enough to graduate to the size category above them (or, sometimes one or two categories beyond that). Sliders decline to a lower category.

One of the more surprising conclusions of this analysis is that the jobs lost from deaths are spread quite evenly across the size categories. Although the smaller firms have a much higher rate of deaths than the large firms, the job losses in the larger firms are much larger for each death. In terms of numbers of firms, there were less than 400 firms employing more than 500 people that ceased operations during 1978-85, but they lost almost 60,000 jobs. On the other hand, the failures of 78,000 firms with fewer than five employees during the period caused only 85,000 people to lose their jobs, or 46% more than the big firms. Many of these, of course, are one-person businesses, the owners of which float repeatedly

into and out of employment and independence.

This indicates the secret of small businesses in their role as the engine of job creation — when they fail, as they often do, the job losses are not too serious, but when they grow, the gains in employment are often impressive. The 5% of the 1978 firms with fewer than five employees that grew into bigger size categories accounted for 15% of all new jobs created during 1978-85. The firms employing 5 to 19 people that grew into bigger size categories were only 1.8% of all the firms of all sizes existing in 1978, but they also accounted for 15% of total job creation.

Perhaps the most impressive conclusion from this analysis lies in the contribution to job creation made by the high growth firms that jumped two or more size categories in 1978-85. Table 9.4 attests to the power of these high achievers.

Table 9.4

The Achievers

Net employment gain by Ontario firms that grew into a size category two or more higher than their 1978 category during 1978-85

Size of firm in 1978 (# employees)	Number of firms: Number	Number of firms: As a % of 1978 total %	Net employment gain: Number	Net employment gain: As a % of total gains in 1978-85 %
<5	820	0.38	38,900	6.1
5 - <20	483	0.22	47,200	7.4
20 - <50	238	0.11	31,700	5.0
50 - <100	14	-	9,300	1.5
Total	**1,555**	**0.72**	**127,100**	**19.9**

Slightly less than three-quarters of one percent of the firms operating in 1978 accounted for one-fifth of all new jobs during 1978-85. These, of course, exclude start-ups during the period, demonstrating the extraordinary potential of small firms to grow fast once they are established.

PART III

The Role of Government in Small Business

CHAPTER 10
THE EVOLUTION OF GOVERNMENT POLICY

When governments first learned to appreciate the importance of their role in nurturing the growth of small firms, their programs concentrated mainly on "how-to" advice to established firms. The business skills of most owners of small firms at that time were generally underdeveloped, so this assistance, delivered mainly by the Federal Business Development Bank, was an important element in raising their ability to operate effectively in an increasingly complex and competitive world.

There is now far less need for government intervention in this area. Not only are modern entrepreneurs much better businesspeople than their predecessors, but they can draw on a broad range of inexpensive, tailor-made advice. Governments still maintain a role in this area, with printed booklets on how to start a business and much more, but it is no longer a primary focus. This is partly why the FBDB is scaling down its management skills training.

The next phase of government policy started when it became apparent that small firms were creating most of the new jobs in the economy. This placed an immediate imperative on the government to nurture such an important resource. The focus in this phase was on financing and on the development of ways to smooth the path of budding businesses. The Ontario government decided to address start-ups as a mass market, starting in 1984-85, and has put in place well-developed start-up assistance. The Ontario government also created the advocacy program to run interference for beleaguered small businesses when other ministries propose laws or regulations that affect them. The Ontario government also embarked on a series of studies to divine what makes entrepreneurs successful. Programs like the Small Business Development Corporations in the early 1980s and New Ventures in the later 1980s made a solid contribution to promoting entrepreneurship. With an average start-up investment of slightly more than $13,000, New Ventures is developing grass roots entrepreneurship. The

Ontario government's counselling program is also providing expert advice in navigating the regulatory and management shoals threatening new and growing businesses.

This phase of government initiative is maturing now. SBDCs have levelled off, although New Ventures is just gathering momentum. With business self-help offices in place across the province, the government can reach for new goals. This doesn't mean it is no longer concerned with start-ups, counselling and financing programs, just that additional programs are being overlaid to add sophistication and depth to Ontario's small business community. Recent innovations include policy thrusts both before and beyond the start-up phase.

One step behind the start-up is the informal investor network, the "angels" who fund new entrepreneurs before they reach the stage when they can draw on commercial financing. Ontarians are only just beginning to find out about these people, who are widely dispersed and keep a low profile, but who are a critical part of the whole process.

Before even that stage, entrepreneurship needs to become known in high schools, which can prepare young minds for the thrills and demands of entrepreneurship. The Ontario government is deeply engaged in developing entrepreneurial options for the high school system. With an experimental new curriculum on entrepreneurship being developed in high schools now and other programs to bring entrepreneurs into the classrooms, young Ontarians are being given an opportunity to appreciate the life of an entrepreneur.

Beyond the classroom and the start-up, the challenges of managing a growing company in today's highly competitive environment are daunting. The major needs of small firms at the beginning of the 1990s are in advanced management skills, in dealing with people and in developing management systems to absorb the mounting flow of raw information.

Once again, there is a role for government to develop an appreciation in small firms of the need for these skills. Effective government programs will help them understand the value of these skills, thereby opening the door to the private sector to deliver these services at higher, commercially viable rates. These comments apply particularly to the technical skills required to keep Ontario firms internationally

competitive. The government has now introduced a program, called Technical Personnel Program, which will help small firms hire the technical expertise they need to keep their operations able to compete effectively abroad.

Finally, there are still gaps in the financing market for small firms. The major one is young firms that are growing rapidly and need equity financing. The existing venture capital industry is not handling this niche, so the government has proposed a program to fill it. Growth Ventures will provide equity capital to the high-risk firms that cannot get by without it.

Overlaid onto this series of policies and programs is the growing need to defend the interests of small business in the waves of legislation that affect all businesses so dramatically. Small business is still not a major priority in Canadian governments, despite its economic importance and they often get caught in crossfire. But then, that's nothing new to them.

CHAPTER 11
GOVERNMENT POLICY ISSUES

The New Ventures Program

The New Ventures program was established in September, 1986. Its primary objective was to provide a source of debt financing to companies that did not have the collateral to support normal commercial loans. Its secondary goal was to encourage start-up ventures to prepare competent business plans and establish adequate financial reporting systems. Applicants for the New Venture loans ware required to submit a satisfactory business plan with their applications.

The program offers a 100% guarantee for loans of up to $15,000 for a term of five years, provided the applicant's equity investment in the business is at least as much as the government guarantee, except in Northern and Eastern Ontario, where the applicant's equity need not be greater than 50% of the loan guarantee. The loan must be for a completely new business and the applicant must commit to hiring at least one employee during the term of the loan guarantee. The program is administered by the lenders, who review and approve proposals.

The program has performed well. Although the take-up of the program was running at an annual rate of about 5,000 new businesses at the end of its third year of operation, compared to a projected 7,000 when the program was instituted, the program's targets were met by a wide margin, as Table 11.1 shows.

Apart from these overall targets, New Ventures had the objective of participation rates in the program of 24% by firms in northern and eastern Ontario and of 24% by women. In the program's first three years, both these targets were comfortably achieved — 29% of the loans went to northern and eastern businesses and 34% went to women.

Table 11.1[1]
Performance of the New Ventures Program

Targets set for the New Ventures program in September, 1986 and actual experience in the period to March 31, 1989

Performance measurement	Targets	Actual
Participants per annum	7,000	4,860
New jobs per loan	1.5	2.3
Annual sales per firm	$45,000	$204,000
Provincial tax per firm	$3,143	$14,307
Private-sector funding	$15,000	$67,700

As of end of March 1989, $120 million in guarantees had been advanced under the program. The average loan was for $13,321. The estimated benefits of New Ventures up to that date were as follows:

Increased sales	$2.1 billion
New jobs (excluding owners)	11,096
Additional tax revenues to the provincial government	$147 million
Additional total investment from the private sector	$356 million

For two-thirds of the successful applicants, their New Venture loan was the first time they had sought commercial financing. Seventy-one percent of them said the program was important or extremely important in starting their ventures and 62% said it was important to the survival of their businesses. Almost a fifth said that, without the program, the chances of their proceeding with their idea would have been less than 25%. However, 61% said there was a 75% chance or better that they would have proceeded with or without the program, mostly by seeking financing elsewhere. The lenders weren't so sure they would have been successful, however. Almost 80% of the lenders reported they would have approved less than 50% of the loans they made under the program on the basis of the borrowers' personal resources. The lenders rated half the applicants as high-risk.

[1] *Report on the Evaluation of the New Ventures Program,* prepared for the Ministry of Industry, Trade & Technology by Price Waterhouse, March, 1989

Despite these odds, the lenders have given the program high ratings. More than half said it had increased their willingness to consider small business loans. Taking this and other considerations into account, it is estimated that about half the loans would not have been made without the New Ventures program.

The average initial investment was $36,188, including owner's equity of $20,373 (68%). Twelve percent of the sample of successful applicants surveyed in the report on the program[2] invested more than $100,000, however. On average, sales of the successful applicants were $173,298 in the first year, $293,990 in the second and $759,487 in the third.

Naturally, the successful applicants for New Ventures were smaller start-ups. Less than 20% are incorporated. However, 7% of the firms had sales of more than $500,000 and they exhibited quite different characteristics than the other firms. More than a third of them (37.8%) were incorporated. They also had initial investments two and half times higher than the average for all firms ($95,115, compared to $36,118) and the owner's equity was double ($41,099, compared to $20,373). They were also more likely to be male, older and better educated. Finally, their income was significantly higher at $40,780, compared to the average for all firms of $30,070, and their net worth was $95,000 on average, more than three times higher than the average for all firms.

The differences between men and women were not widespread, although they did follow some of the patterns identified earlier in this report. The average earnings of the women were $23,866, compared to $33,257 for the men. And in the survey of successful applicants, the women invested much less ($67,788, compared to $94,417 by men). These figures are not representative as the survey showed higher investments than the analysis of all loan applicants. However, they do illustrate trends. The women were also twice as likely to have partners as the men (39% compared to 21%) and they created fewer jobs — 1.4 employees compared

[2] Ibid. *Report on the Evaluation of the New Ventures Program*

to 2.7 by the men. However, only 28% of the defaulted loans were to women, although women represented 34% of the borrowers.

The effectiveness of New Ventures in encouraging more business planning was mixed. They were prepared for the requirement to submit plans, because 82% of the successful applicants said they had made a business plan before applying and 90% had made cash flow or sales projections. And they found them moderately useful. As a result of the process of filling in the application form, 42% changed their assessment of start-up costs and 40% changed their assessment of their operating costs. Forty percent changed their assessment of financing needs for the business.

Almost half the applicants (46%) said the discipline of preparing a business plan had helped them understand planning better and 49% felt it had helped them establish a better relationship with the lender. However, they didn't think the planning process had helped them much in understanding the competition (66%).

Loan losses to the end of March 1989, were $9.5 million, which was far below projected defaults when the program was started. It appears that, on average, only 20% of the loans will be in default by the end of their third year. This is a significantly better rate than the whole population, almost half of which have ceased to operate at the end of their third year, as Chart 11.1 shows.

These figures may be revised when the program has been in effect for longer, because it is not mature yet. It is estimated that annual costs will rise to between $19 million and $25 million by 1993-94, depending on the number of applicants and economic conditions.

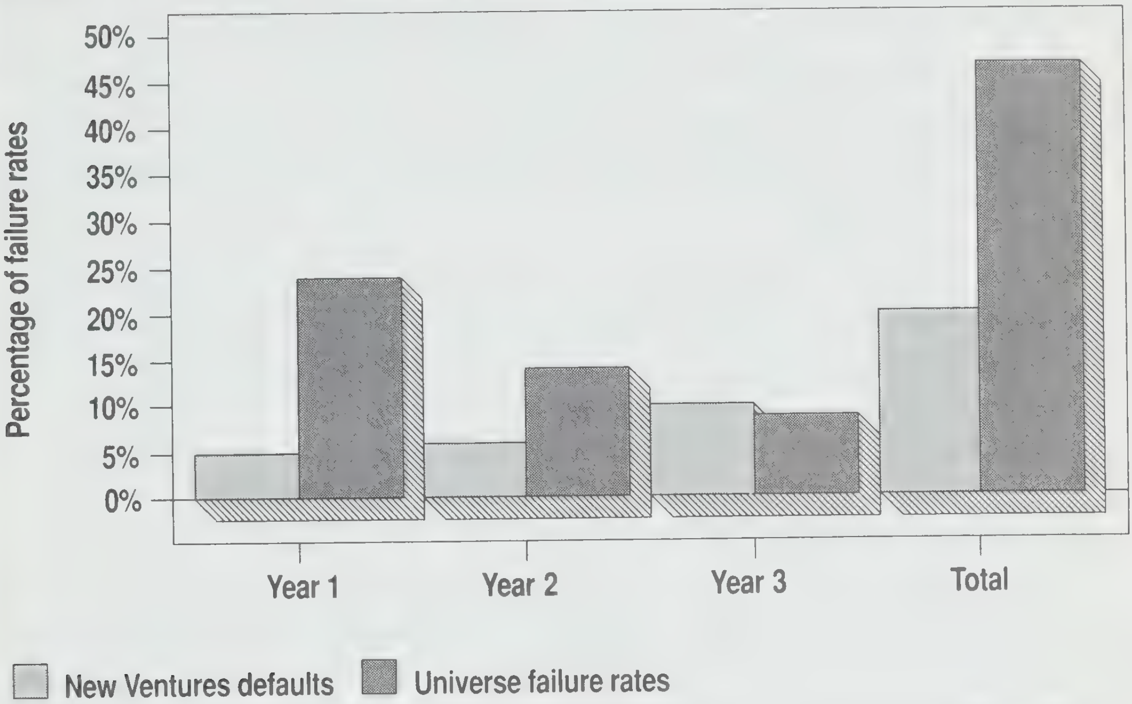
Growth Ventures

The other side of the New Ventures coin is Growth Ventures, a new program announced by the Ontario government last spring. It is a new form of assistance in raising equity financing for growing small and mid-sized companies in Ontario.

Chart 11.1

New Ventures Loans Fail Less Often than the Average

Comparison of failure rates in the first three years after start-up for all firms in Ontario and for successful applicants in the New Ventures Program



The program is a response to the need expressed by young growing companies for equity capital. In a survey conducted for the Premier's Council[3], lack of equity capital was cited as a constraint on growth by 74% of the companies. Lack of debt financing was identified as a constraint by 59% of the companies. It has long been recognized that smaller firms, particularly growth firms, are more heavily leveraged in their financing than large companies. The Economic Council of Canada found that firms with annual sales of less than $25 million had a debt/equity ratio of 55:45, compared to 41:59 for the remainder.

At times of recession or high interest rates, overleveraged companies are the first to suffer because they cannot sustain their payments of loan interest in the face of a prolonged drop

[3] *Competing in the New Global Economy*, Report of the Premier's Council, Volume 1, citing results of the survey conducted by the Canada Consulting Group and Telesis.

in revenues. Because these firms are riskier investments, investors demand a higher return or a level of ownership that is unacceptable to the entrepreneur. There are two effective ways of reducing this high level of risk:

- Pool investments in these kinds of firms so that the successes can support the failures.
- Leverage the equity investment of the pool by giving them access to low-cost loans that can make their equity dollars stretch further.

Growth Ventures is aimed at reducing risk through these kinds of measures. It will augment pools of privately-owned investment capital that make equity investments in the small and mid-sized firms the government wants to help. Investment decisions will be made by the operators of the pools, who will be approved by the government as participants in Growth Ventures.

The program will be administered by the Ontario Development Corporation, which will announce details of the program in the new year. The Ontario Development Corporation will guarantee loans to the operators of the pools of money in order to make their equity dollars stretch further. Interest rates on the guaranteed loans will be at or slightly more than the current rate for Ontario government bonds.

A key component of these kinds of investors is that they should ideally participate in the management of the venture since the competence of the entrepreneur is critical to its success. Few Canadian venture capital companies are structured to provide this kind of assistance. Most of the Canadian venture capital industry has moved away from early-stage development and are not acting as an effective intermediary between the large institutional sources of venture capital and the growing companies.

The Small Business Development Corporations met an important need for financing growing ventures, but this program is levelling off now. Net registrations of SBDCs (new registrations less revocations) were -11 in 1987-1988 and only +15 in the first nine months of the most recent year. The SBDCs also have tended to meet the needs of the informal

investor market[4], whereas the government wants now to help develop the formal venture capital market. The pool approach will help equity financing in the one range where there is a significant gap in the market — smaller, growing firms.

Educating Future Entrepreneurs

The Ontario government has embarked on a major project, still in the pilot stage, to heighten awareness of entrepreneurship among elementary and high school students (See The State of Small Business, Ontario, 1988). There are currently two major policy initiatives being developed:

- The Ministry of Industry, Trade & Technology will start two pilot projects in early 1990 for a new program called VISIONS. This project is aimed at students in grades seven and eight, who will be given an opportunity to meet real entrepreneurs in their classrooms. The entrepreneurs will be encouraged to share with them their dreams, motivations, challenges and problems. The Ministry is preparing teaching aids for both teachers and entrepreneurs to maximize the effectiveness of the encounters.

- The Ministry of Education has developed a curriculum called Entrepreneurship Studies for grades 11 and 12. The main objective in the curriculum is to enable these students to assess their personal interest in and aptitude for entrepreneurial activities, but the benefits are expected to extend toward helping them think creatively in a wide range of fields, including their choice of career and life skills.

  The project is still in the pilot stage. Of the province's 767 schools, 40 taught the course in 1988-89. The Ministry of Industry, Trade & Technology is actively involved in the implementation of this curriculum. The major difficulties that have come to light are the training of qualified teachers and development of teaching materials.

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[4] An Equity Financing Vehicle for Growth Companies, a report prepared for the Small Business Branch of the Ministry of Industry, Trade & Technology.

These programs are being developed in the light of a survey of attitudes among schoolchildren in Ontario aged 12 to 18. This survey demonstrates strongly positive, if somewhat idiosyncratic, attitudes toward small businesses and entrepreneurs. The highlights of the report[5] include:

- More than half the students think most businesses employ more than 100 people;
- Only 18% thought small businesses create most new jobs;
- They are more perspicacious in their view of what entrepreneurs are. More than half thought they were owners of small businesses and 36% thought they were managers of businesses. Just less than 30% thought they have ideas on how to make money or they have ideas on new products or they bring together workers, money and a product or service. Almost a quarter thought they recognize and act on opportunities, and 16% thought they were presidents of big companies;
- Small business has a very positive image among high-school students, 81% of whom think entrepreneurs get along well with people. Seventy percent think entrepreneurs want to help workers get training and 61% think they treat all people fairly. Sixty percent think they are honest (but 28% thought they weren't). The students were evenly split on whether entrepreneurs are interested only in making money;
- Forty-three percent of the students said they were likely or somewhat likely to start a new business. This tendency was stronger among students who like school than among the 30% of them who don't;
- There were few significant differences in the responses of male and female students. However, when asked if they were likely to start a business when they finished school, 16% of the males said that was very likely, compared to

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[5] *Survey of Student Attitudes on Entrepreneurship and Small Business*, September, 1989, conducted by the Ministry of Industry, Trade & Technology, with the assistance of Environics Research Group.

11% of the females. And 11% of the males said it was not at all likely, compared to 15% of the females; and

- Forty-six percent said a member of their extended family currently owns a business.

The survey was conducted with 929 students in 19 schools in Thunder Bay and in East York in Metropolitan Toronto.

A Training Levy on Payroll?

The Advisory Council on Adjustment, chaired by Jean de Grandpré, has suggested that Canadian companies be encouraged to allocate more resources to training their employees by a refundable levy of 1% of payroll. The levy would be refunded to employers who spend the required amount of money on employee training.

The cost to Ontario small firms is projected to be $374 million, or about $218 yearly per employee. Two different surveys have found differing opinions on the training effort of small firms[6]. The Canadian Federation of Independent Business found that the training effort increases as firms grow bigger, rising from 66% in firms with fewer than 20 employees to 84% of those with more than 50 employees. The Ministry of Skills Development found that 27% of all Ontario firms have formal training programs, but the effort is much greater among firms with 20-49 employees (53%) and 50-199 employees (61%).

The difficulty in assessing training outlays precisely lies in the nature of employee training in small firms, because so much of it is on-the-job. This is expensive in the time of other employees or of the owners, but the cash outlays are much lower, even relatively, than they are in big companies with institutionalized training systems. Because the training outlays of small firms are more difficult to measure, the training levy would favour organizations with formally structured training systems, resulting in small firms bearing a disproportionate share of the tax.

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[6] *Skills for the future: Small Business and Training in Canada,* Canadian Federation of Independent Business, March, 1989. The Training Decision: Training in the Private Sector, the Ministry of Skills Development, April, 1989

There is also a problem in defining who is an employee and who is self-employed in the construction, trucking and several other industries.

Self-Employment and the Workers' Compensation Board

The trend toward self-employment is causing some administrative problems for government agencies responsible for collecting premiums or taxes. The Workers' Compensation Board, for example, believes it is losing up to 10% of its premium income from independent sub-contractors who are eligible for WCB benefits but escape paying premiums. This arises despite an arrangement between the WCB and the major trucking and logging firms, which have agreed since 1976 to remit WCB premiums on behalf of the independent truckers after deducting the appropriate amounts from their payments to the truckers. The Board has proposed solving the problem by defining these self-employed sub-contractors as employees, and making their major (or sole), client responsible for them as far as the WCB is concerned.

The WCB proposes to apply an "organization test" that would define independent contractors as employees if their operations are considered an integral part of their clients' businesses. This would run counter to the provisions of the Truck Transportation Act, which recognizes owner-operators as independent business people.

Revenue Canada's current definition of self-employment requires that there be no master-servant relationship, and that the means of production be owned by the self-employed person, who should have a reasonable expectation of profit or risk of loss.

With an increasing number of employees choosing to become self-employed, and a growing realization in big business that working with independent sub-contractors is often more efficient and inexpensive, there is a lot at stake in how self-employment is defined.

There are more than 100,000 self-employed people in Ontario who have no employees. The most important sectors for these people are construction contractors (30,000), owner-operators in the trucking industry (15,000) and people providing services to business (21,000).

The Goods and Services Tax

The proposed federal Goods and Services Tax (GST) has been welcomed by many business organizations because it will replace the federal sales tax, which is generally regarded as unsatisfactory. However, very few business organizations are comfortable with the specific design of the GST. Small business organizations and many sectoral business associations feel the rate is too high because there are too many exemptions. There is concern at the complexity of the tax system, particularly if the federal and provincial governments run parallel sales taxes, applying different rates to different ranges of goods and services. Many aspects of the GST are complex and will demand outside advice for small firms.

The federal government has made a number of concessions to the difficulties of small businesses. Firms with sales less than $6 million a year will be permitted to remit their tax to Ottawa quarterly and procedures will be streamlined for retailers with revenues of less than $2 million a year. And the government will credit collecting organizations with a fee for administering the tax. The credit will be 0.4% of sales to a maximum of $600. While these measures are helpful, they will fall far short of compensating small firms for the extra work.

The GST will mean as many as 150,000 Ontario businesses will collect sales tax for the first time. The biggest danger in this sudden expansion of tax collectors is that some people will drift into the cash economy, thereby reducing both GST and the personal income tax yields, because of unreported income.

Personal and household services may be negatively affected by the tax, since they are usually paid out of discretionary income. This industry is also the most vulnerable to a growth in the underground economy.

The other concern for small firms is their sales to tax-exempt organizations. Tax-exempt clients of small firms include dental and health services, daycare, legal aid, educational services, the public sector, domestic financial services, and the MUSH sector (municipalities, universities, schools and hospitals). The danger is that these organizations do not pay any GST and they do not receive any credit on the GST component of goods and services they buy. This means their

suppliers are at a disadvantage in price terms against employees of the tax-exempt organization who can provide the same service without paying GST on it.

The MUSH sector is partly protected from this danger because credits are available to them up to what they would have paid under the federal sales tax. Small firms would prefer the others be classified as zero-rated, which means that they are eligible for rebates on the GST components of goods and services they buy from suppliers.

Technical Personnel Program

As part of the government's continuing program to improve the competitiveness of Ontarian companies, it introduced in the late summer of 1989 a new program called Technical Personnel Program (TPP). This is designed to reduce the financial barriers to hiring appropriate people in small firms that lack technical expertise. The program provides one quarter of a technical employee's salary over a three-year agreement, to a maximum of $45,000 per person.

The program is aimed specifically at upgrading the technology of the company. The grant can be applied to projects to improve product quality, production processes, the facility layout or develop new products or services, among other eligible purposes. These projects will assist companies to compete in the export market. The critical requirement is that the company not have anyone with the required expertise on staff. The grant will be 50% of the first year's and 25% of the second year's salary, subject to a maximum salary of $60,000.

The program is not available to companies that wish to upgrade their employees' skills for general purposes. They must have a specific project, fully costed, to improve the quality of their goods or services or their production processes. Other eligibility requirements include:

- The company must be a manufacturing or service company based in Ontario (no retail businesses are eligible);
- it must have 10-200 employees;
- the company must be at least two years old;
- it must be exporting or have plans to export the products for which the technical personnel are needed;
- the company must commit to a three-year program; and
- the technical person must be a new hire.

APPENDIX: SMALL BUSINESS ADVOCACY REPORTS

These research reports are available from Small Business Advocacy, Ministry of Industry, Trade and Technology, 7th Floor, Hearst Block, 900 Bay Street, Toronto, Ontario M7A 2E1 (416) 965-6304.

1. **Survey of Small Business Registrants, 1984 (October 1984)**

   Results of interviewing 911 Ontario entrepreneurs about the businesses they start. Includes information on investment, hiring intent, previous experience, type of business, why the business was started and demographics.

2. **Self-Directed RRSP Investment in Private Companies (May 1985)**

   Survey of characteristics of holders of self-directed RRSPs (150 people). Results compared to information obtained from 2,000 people when they either opened self-directed RRSPs or transferred funds to such an RRSP. Survey was conducted on behalf of SBA by Decision Marketing Research Limited.

3. **Expanding Ontario's Small Business Development Corporations Program to Business Services (May 1985)**

   Argument for extending eligibility under Ontario's SBDC program to Ontario's business service firms. Also argues for expansion of SBDC's existing Match-up Service to introduce appropriate SBDC investors and small business owners and emphasize smaller placements of equity.

4. **An Advance Notice System for Proposed Regulatory Initiatives (September 1985)**

   Proposal to create an Advance Notice System in Ontario. Includes an examination of advance notice in place in other jurisdictions, description of Ontario's history with respect to advance notice, identification of principles to be considered in any improvement of the regulatory process and policy options and recommendations.

5. **Newly-formed Small Businesses in Ontario, 1982-84 (August 1985)**

   Results of interviewing 861 Ontario entrepreneurs. Provides a profile of Ontario's small business owners and their attitudes about various issues and programs, as well as a comparison of unincorporated and incorporated businesses. As well, the research provides a profile of the kinds of businesses that are started and remain viable. Survey was conducted on behalf of SBA by The Creative Research Group.

6. **Small Business Payroll Taxes (March 1986)**

   The economic implications of payroll taxation on small businesses are examined. Also looks at the effects of abolishing Ontario Health Insurance Plan premium payments and replacing the payments with a 2% employer-paid payroll tax. Features an examination of impacts on an average small business, a garage, a restaurant, a construction firm and a manufacturer.

7. **Small Business Regulation and Paperburden (March 1986)**

   A joint project of SBA and the Department of Regional Industrial Expansion, Ontario Region, the study identifies and clarifies specific areas of regulatory and paperburden in Ontario's small business community. Looks at problems and problem sources identified by the general economic sectors and more specifically the tourism sector. Survey was conducted by The DPA Group Incorporated.

8. **Entrepreneurship and Small Business (May 1986)**

A discussion paper tabled in Ontario Legislature by the Minister of Industry, Trade and Technology, the Honourable Hugh O'Neil, as a supplement to the Ontario Budget of April 1986. Describes: entrepreneurship in Ontario, new business formation and small firm performance.

9. **The Ontario Investment Network (April 1986)**

Describes the rationale for the establishment of the Ontario Investment Network (presently operated by the Chamber of Commerce under the name Canada Opportunities Investment Network - COIN). Discusses the chronic shortage of equity capital suffered by the small business community across Canada.

10. **New Small Businesses (April 1986)**

The 1986 survey of new unincorporated business starts. The results of 1,118 interviews show the age, sex previous ownership and employment experience of new business owners as well as the reasons for starting the business. The study also breaks down the start-ups by sector and expected billings and source of investment.

11. **New Ventures: A Loan Guarantee Program for New Businesses in Ontario (June 1986)**

Describes rationale for the New Ventures Program, announced in the Speech from the Throne in April 1986. Discusses access to financing problems of small businesses. Shows design of the New Ventures program including details on eligibility criteria, program administration, roles of co-sponsors, application processes and costs of program. A project of the Committee of Parliamentary Assistants for Small Business and Rick Ferraro, Small Business Advocate.

12. Small Business Capitalization and Proposed Pension Investment Reforms (August 1986)

SBA submission to the Pension Commission of Ontario regarding the policy recommendations for the regulation of pension fund investments. Argues for expanding the universe of eligible pension fund investments to include more small businesses. Includes copy of the Pension Commission recommendations.

13. Targetting Employee Share Ownership Plans to Small Business (September 1986)

Describes the rationale for targetting the Employee Share Ownership Plans program (announced in the June 1986 Budget) to small businesses. Provides recommendations on how the plan's optimum use by the small business community may be encouraged.

14. Workers' Compensation Experience Rating: A Claim Deductible Concept (October 1986)

The study examines the feasibility of introducing a concept of a claims deductible into the experience rating of claims costs under Workers' Compensation in Ontario. Study was conducted on behalf of SBA by William M. Mercer Ltd.

15. Hours of Work and Overtime in Small Businesses: Five Case Studies (December 1986)

Case studies of hours of work and overtime practices in five Ontario firms: sewer and water main contracting, clothing manufacturer, courier and moving service, lumber and building supply and weigh scale repair and distribution. Qualitative research on attitudes of owners towards overtime and data on firms and their practices.

16. The State of Small Business (December 1986)

The first annual report on small business in Ontario. Features data on: the job creation record and growth of small business, profiles of the small business owner, franchising, women business owners, the aspirations and achievements of new business owners, small business financing and effects of public policy on the small business community. Tabled in the Ontario Legislature in December 1986 by the Minister of Industry, Trade and Technology, the Honourable Hugh O'Neil. A project of the Committee of Parliamentary Assistants for Small Business and Rick Ferraro, Small Business Advocate. Available in French as *La Situation des petites entreprises.*

17. University Centres of Entrepreneurship for Ontario (February 1987)

Describes rationale for the establishment of centres of entrepreneurship in Ontario universities. Included in the April 1986 Speech From The Throne.

18. Ontario's Fast-Growth Companies (April 1987)

Examines the characteristics of 84 successful Ontario entrepreneurs. Study conducted on behalf of SBA by Decision Marketing Research Limited.

19. Small Business Payroll Taxes, 1987 (March 1987)

The 1987 update of the 1986 Small Business Payroll Tax study. Focuses on the increasing burden Workers' Compensation places on small businesses.

20. The Status of Female Employees in Small Business (June 1986)

Survey of 353 Ontario small business owners (in the manufacturing sector) regarding the status of women in their firms. Examines employment patterns, wage and salary administration, personnel practices and company policies. Also looks at which form of pay equity legislation would least affect the viability of small businesses. Survey was conducted on behalf of SBA by Hay Management Consultants.

21. **Pay Equity and Ontario's Small Business Sector (June 1986)**

Survey of 302 Ontario small business owners (representing all industrial sectors) regarding the types of personnel practices they follow in their firms. Also includes results of 16 interviews with persons knowledgeable about pay equity and small business regarding how to implement pay equity in small businesses. Survey conducted on behalf of SBA by Urban Dimensions Group Inc.

22. **Business Transfer Tax: Modelling the Impact on Small Firms (November 1987)**

Study demonstrates how profits and sales in several Ontario small businesses might be affected by the federal government's proposed business transfer tax. Examines eight types of businesses: retail florists (unincorp. and incorp.), retail drug stores (incorp.), retail jewellery stores (incorp.), rubber processors and suppliers (incorp.), fan and ventilator manufacturers (incorp.), engineering processing firms (incorp.) and lodges and motels (incorp.)

23. **Business Starts in Ontario: An Econometric Analysis and Forecasting Model (August 1987)**

Reports on the determinants of new business starts, including changes in population and labour force, industrial structure and rates of unemployment output growth, costs of borrowing and inflation. Includes a computer-based forecasting model for the next five years. Study carried out by Quantec Research Ltd.

24. Hours of Work and Overtime in Small Business (January 1988)

Compares a sample of 300 small firms (fewer than 100 employees) with control group of 60 large firms to assess the impact of recommendations proposed by the Task Force on Hours of Work and Overtime submitted in May 1987. Finds that the proposals are unlikely to have a significant effect on overall average hours worked per week in Ontario, but that some of the recommendations affect small and large firms differently. Small businesses are relatively more affected by proposals to shorten the regular work week from 44 to 40 hours.

25. Facilitating the Investment of Self-Directed RRSP Funds in Small Businesses (July 1988)

Examines amendments to the federal Income Tax Act in 1986 permitting holders of Registered Retirement Savings Plans (RRSPs) to invest in small and developing businesses. Recommends simplifying the rules and shifting the burden of compliance from financial institutions to the involved parties. Contends that these changes will increase RRSP investments in small businesses.

26. Safety Matters: Case Studies of Health and Safety Practices in the Workplace (September 1988)

Case studies of 13 companies (of which six had fewer than 100 employees) examining the differences in approach between large, medium and small firms. Discloses that the larger the company, the more extensive its formal health and safety program. While larger companies have well-developed corporate health and safety philosophies, small firms tend to do positive things in the workplace because the owners care about their employees' welfare and are sensitive to the disruption an accident can cause.

27. **Newly-Formed Small Businesses in Ontario, 1985-87 (August 1988)**

Based on interviews with 1,055 small firms, updates the August 1985 report on newly-formed small companies. Focuses on management, operational and policy issues for both incorporated and unincorporated firms. Special efforts were made to increase the sample size of companies having more than 20 employees in order to better understand the phenomenon of growth. Discloses that finding and keeping qualified employees is now the top-rated barrier facing young companies.

28. **Employment Standards in Small Firms (March 1988)**

By a telephone survey of 307 small Ontario businesses and a control group of 25 larger firms, examines employee compensation issues, including possible changes to the minimum wage, training, benefits, vacations and leave arrangement, subcontracting and contracting out, and retirement policies.

29. **An Equity Financing Vehicle for Growth Companies (January 1989)**

Discusses a possible Ontario investment vehicle to improve the equity financing of companies with growth potential. Applies the U.S. model of small business investment companies, under which the government guarantees debentures issued by investment companies that specialize in small business. This approach, successfully practiced in the U.S. since 1958, was responsible for the genesis of much of the American venture capital industry. It enabled venture capital firms to multiply their capital under management and operate at a scale sufficient to build up the investment, management, and marketing expertise necessary to manage a portfolio of growing firms.

30. The State of Small Business, 1987 (December 1987)

The second annual report on small business in Ontario. Features the Committee of Parliamentary Assistants for Small Business' proposal for a small business impact statement (SBIS) to set out in cabinet submissions the impact on the small business community of proposed changes in Ontario policy, legislation and regulations. Concentrates on the dynamic growth of small businesses in Ontario and includes research findings on where the jobs are coming from, the performance of successful young companies, remaining barriers to growth and the government's response.

31. Survey of Student Attitudes on Entrepreneurship and Small Business (September 1989)

Survey of 929 students in Grades 7 & 8 and Grades 11 & 12 examines student attitudes on entrepreneurship and small business. The survey was conducted among students in Thunder Bay and East York. It investigates students' awareness and knowledge of small business, perceptions of small business owners and the likelihood of starting their own business in the future. Environics Research Group Limited analyzed the data.

32. The State of Small Business, 1988 (January 1989)

The third annual report on small business in Ontario. Features a bilingual small business owners guide as well as data on job creation. Concentrates on growth opportunities with specific reference to exporting, high technology, and government procurement. Small business financing is also highlighted.

33. Report on the Evaluation of the New Ventures Program (March 1989)

Review of Ontario's New Ventures Program by Price Waterhouse. New Ventures has assisted more that 13,000 new businesses in accessing over $160,000,000 in private sector financing during the past three years. The analysis outlines user and lender profiles, the program's costs and benefits as well as projections for future costs.

34. Business Ownership for Women (BOW) Review (August 1989)

Review by Ivy Lea Consultants of the Ministry's BOW Program. The program, which comprised fifty seminars and seven conferences, ran from September 1985 to 1988. The report assesses the effectiveness of the program and recommends future government programming in support of women entrepreneurs.

35. University Small Business Consulting (USBC) Review (October, 1989)

Review by the DPA Group Inc. of the Ministry's USBC Program. The USBC program offers low cost student consulting services to local small businesses. The service is provided from May to the end of August each year at 15 Ontario universities. The review assesses the effectiveness and value of the program.

36. Managing People in Small Business (August 1989)

Report of six focus groups conducted with small business owners and those involved in managing people. Its purpose was to explore initiatives that MITT might undertake to improve human resource management in Ontario's small businesses. The conclusion was that there is a need for a well-developed multi-faceted program with direct proactive marketing.

Ministry of
Industry,
Trade and
Technology

Province of Ontario
Queen's Park
Toronto, Canada
M7A 2E1

Monte Kwinter
Minister

SMALL BUSINESS ONTARIO

The State of Small Business

VT INCEPIT FIDELIS SIC PERMANET
Ontario

1990 Annual Report on Small Business in Ontario

MINISTRY OF INDUSTRY, TRADE AND TECHNOLOGY

Enquiries regarding this publication should be directed to:
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	Excellent	Good	Fair	Poor
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Information on government programs and policies				
Other				

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The State of Small Business

VT INCEPIT FIDELIS SIC PERMANET
Ontario

1990
Annual Report on Small Business in Ontario

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Ontario

Minister of Industry, Trade and Technology

It is my pleasure to present the fifth edition of **The State of Small Business**. Each year since 1986, my Ministry has prepared the definitive statement on small business in Ontario.

As in previous years, the 1990 edition highlights the contributions that small businesses make to our economy. It also looks at the government's responses to the needs of small businesses in the areas of finance, education and assistance in technology.

I am sure that anyone with an interest in this subject will find this to be a useful and informative book.

Allan C. Pilkey

Allan C. Pilkey, M.P.P.
Minister

CONTENTS

ACKNOWLEDGEMENTS

The Government of Ontario would like to recognize the people who have contributed to the fifth edition of *The State of Small Business*.

The project was designed and written by Donald Rumball, in co-operation with Rena Blatt, Research Advisor in the Ministry of Industry, Trade & Technology's Small Business Ontario. Other members of the staff of Small Business Ontario also contributed significantly, including Jeffrey Stutz, Manager of Small Business Advocacy,
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THE STATE OF SMALL BUSINESS ONTARIO, 1990 EXECUTIVE SUMMARY

PART I

Small business in Ontario's Economy

In the 1980s, Canada enjoyed the second fastest economic growth of all the major developed countries, surpassed only by Japan. The engine of this growth was Ontario, which has created a record number of new jobs in the process. Although the number of employees dipped during the 1981-82 recession, as might have been expected, employment recovered strongly during the balance of the decade, finishing up 17% ahead of 1981. Unemployment in 1989, at the decade's end, was at 5.5%, compared to 7.7% for Canada.

Self-employment grew even more strongly, increasing by 40% in Ontario during the 1980s. The self-employed now represent about one in seven of the people actively employed. These entrepreneurs are the source of the driving force behind the hundreds of thousands of small firms that, between them, accounted for three quarters of the new jobs created in Ontario during the decade ending in 1988.

As the decade ended, however, some of these employment gains began to slip away. By September of 1990, actual and announced layoffs of 50 or more people had reached a combined total of more than 25,000, compared to about 46,000 in 1982. Disturbingly, however, the layoffs in 1990 had a much higher component of permanent closures of plants or portions of plants - 60%, compared to a quarter in 1982.

As this report went to press, it was not clear how deep the 1990 recession would be, but there was concern that companies, consumers and governments all had a great deal less room to manoeuvre going into the 1990 recession than they did going into the 1981-82 recession. Between them, they borrowed more than $700 billion during the 1980s. Consumer debt doubled in the six years to 1989, and residential mortgages increased 117% in the decade to 1989.

Consumers accounted for 26% of the $711 billion of debt incurred between 1980-89. Big businesses accounted for 19%, the federal government for 31½%, other governments for 17½% and small and mid-sized

firms for 6%. In 1989, corporate profits (which are dominated by big firms) were only 57% higher than in 1981, while big-company debt was up 140%. This means that, compared with the last year before the last recession, big firms are now carrying 50% more debt for each dollar of profit. Small firms, by contrast increased their debt load only 50% during the decade.

Unincorporated businesses were even more conservative. Their net income was up 153% during the 1980s, while outstanding debt rose 33%. This means that, compared to 1981, small, unincorporated firms are now carrying about half the debt they carried in 1981 for each dollar of profit.

The significance of this overhang of debt is heightened by the extraordinarily high real interest rates (taken as prime rate less the rate of inflation). Since the 1981-82 recession, real prime rate stayed above 5% for all but 20 weeks, averaging 6.7% over the period. In 1990, real prime did not go below 8% for the first 10 months at all, averaging 9%.

An additional pressure on businesses in Canada is the globalization of markets, particularly through the Free Trade Agreement with the U.S. This is having a strong effect on retailers, who are losing business to the U.S. border cities, where prices are much lower. About 13% of Ontario's population live in border areas, so the lost business has a significant effect. It is estimated that Canadians who cross the border to shop in the U.S. may be draining up to $500 million in retail sales from domestic outlets. The provincial government is losing almost $50 million in tax revenues.

A decade of remarkable growth

In the decade between 1978 and 1988, small firms accounted for 74% of all the new jobs created in Ontario. This enabled small firms, defined as those employing fewer than 100 people, to raise their share of the workforce to 34% from 31%, mostly at the expense of big employers, whose share declined to 50% in 1987 from 54% in 1978.

The most significant contribution to job creation came from the smallest firms, which employed fewer than 5 people. (Many of them grew into larger firms, but they had fewer than five employees when they started out.) These firms accounted for less than one fifth of small-business employment in 1978 but contributed almost half a million new jobs, or half of the jobs created by small businesses between 1978 and 1988. That's a growth rate of 125% over the ten years, an average of 8½% a year, or more than double the average annual growth in the Gross Domestic Product.

SMALL BUSINESS FACT SHEET (1)

All employers		**Canada**	**Ontario**
Number of firms, 1987			
Total		885,635	304,397
By firm size	- small	874,197	297,806
	- medium	9,162	4,997
	- large	2,276	1,594
Small firms as a % of total		98.7%	97.8%
Increase in the number of firms, 1978-88			
Total		47.4%	41.2%
By firm size	- small	282,542	87,630
	- medium	1,914	1,122
	- large	360	130
Small firms as a % of the total		99.2%	98.6%
Annual growth	- small	4.4%	3.9%
	- medium	2.6%	2.9%
	- large	1.9%	0.9%
Number of jobs, 1987			
Total (000s)		11,181	4,600
By firm size	- small	4,138	1,562
	- medium	1,746	726
	- large	5,297	2,312
Small firms as a % of the total		37%	34%
Net gain in jobs, 1978-88			
Total (000s)		2,739.5	1,354.7
Increase over 1978		29.9%	37.9%
By firm size	- small	2,224	1,000
	- medium	270	157
	- large	246	197
Small firms as a % of the total		81%	74%
Annual growth	- small	5.6%	6.7%
	- medium	1.7%	2.6%
	- large	0.5%	1.0%
Average salaries, 1987			
Small firms (<20 employees)		$12,182	$13,223
Small firms (20-99 employees)		$17,425	$19,021
Mid-sized firms (100-499 employees)		$21,136	$22,372
Big firms (500 or more employees)		$24,679	$25,528
All firms		$19,567	$21,082

Notes: 1. Small firms employ fewer than 100 people, medium-sized 100-499, large firms more than 500.

2. The number of jobs is full-time equivalent - part-timers are counted as a fraction of full-time.

3. The 1988 statistics are accurate for the total number of jobs and firms, but not for the distribution by size of firm. Whenever distribution by firm size is involved, 1987 statistics have been used.

SMALL BUSINESS FACT SHEET (2)

The market sector		Canada	Ontario
Number of jobs, 1987			
Total (000s)		8,458.4	3,613.1
Small-firm share		44.4%	39.9%
Goods-producing sector		2,922.5	1,341.3
Trade sector		2,091.1	853.4
Market services		3,405.0	1,402.4
Small-firm share	- goods-producing	38.2%	33.5%
	- trade	53.3%	48.0%
	- market services	43.7%	40.4%
Net gain in jobs, 1978-88			
Total (000s)		1,992.4	867.3
Total (%)		28.2%	35.5%
Share of total by firm size:	- small	98.5%	89.3%
	- medium	7.8%	12.3%
	- big	-6.2%	-1.7%
Sectoral share:	- goods-producing	19.0%	24.8%
	- trade	32.8%	30.1%
	- market services	48.2%	45.1%
Small-firm share within sectors	- goods-producing	153.2%	114.6%
	- trade	79.4%	75.0%
	- market services	90.9%	85.0%
Annual growth by firm size:	- small	5.5%	6.6%
	- medium	1.3%	2.5%
	- big	-0.4%	-0.1%
Births and deaths			**Ontario**
Number of firms, 1978			215,472
Startups, 1979-88			409,604
Failures, 1978-87			309,725
Startups with <20 employees (% of total)			97.4%
Failures with <20 employees (% of total)			97.3%
New jobs created, 1978-88			1,354.9
Jobs created by startups, 1979-88			1,159.2
Jobs lost from failures, 1978-87			626.6
Survival rate, after 1-10 years in business:	1		77%
	2		63%
	3		53%
	10		23%

Notes: 4. Average salaries are calculated on the basis of individual labour units, which counts part-time workers as a unit, not a fraction.

5. The market sector is defined as all industries other than those funded by governments or their agencies. The latter include education, health and welfare, religion and public administration.

6. Source: Based on data generated by Small Business and Special Surveys division, Statistics Canada.

Equally strong gains in employment were enjoyed in the funded sector, which encompasses governments and their agencies, including education and health and welfare. In the ten years, 1979-88, employment in the funded sector grew by 36% in Canada, accounting for 27% of the new jobs during the period. By contrast, the market sector grew by 28% to account for the remaining 73% of the new jobs. The funded sector has grown significantly faster in Ontario (48%) than it has in the rest of Canada (29%) over the ten years to 1988. Moreover, the funded sector is largely responsible for whatever growth there has been in large organizations. The funded sector accounted for 27% of the new jobs during 1979-88, but 94% of the new jobs in firms employing more than 100 people.

The importance - and fragility - of new venture formation

On average, almost a quarter of new firms fail within the first year of their lives; by the end of the third year, about a half are no longer in business. In any one year, firms that die in their first year of operation account for 30% of the jobs lost by deaths. At these rates, the average life expectancy of a new firm in Ontario today is 8 years.

Despite this enormous turnover, however, "births" are a critical element in the job-creation process, accounting for 107% of total new jobs created in the market sector during the decade to 1988. Expansions of firms that already existed in 1978, by contrast, accounted for 97%. Small firms, not surprisingly, assume a dominant role in births, accounting for 84% of the jobs created by births in the market sector.

In the past decade business formations have grown strongly. Between 1979 and 1987, startups increased by more than a quarter to almost 50,000. In the same period, registrations (which measure intention of starting a new venture), increased nearly two and half times to almost 120,000. Then the growth stopped. Startups stagnated in 1988 (the latest accurate figures), while registrations declined almost 30% over the following two and a half years, to reach an annual rate of 92,000 in the first eight months of 1990. Since registrations have generally been predictive of startups, it seems likely that, when updated statistics are made available next year, startups will be shown to have declined significantly in 1989 and 1990, posing a threat to the continuation of the high level of job creation.

An additional danger sign is the level of failures. In the period up to 1985, failures followed a fairly predictable course, moving with economic conditions, but failure rates started rising in 1986. In 1987, these rates jumped sharply to three or four percentage points higher than they had been

during the previous decade, indicating a general deterioration in the resilience of small firms that goes beyond any increased volatility of younger firms.

The end of an era?

From 1984 onwards, the share of total job creation credited to small firms rose from 72% in 1984 to 91% in 1987. Then, in 1988, there was a sharp reversal as big and mid-sized employers reasserted themselves, adding almost 3½% to their workforces after growing at only slightly more than ½% a year during the previous two years. Employment growth in 1988 in the funded sector was more than three times the average annual growth rate of the previous four years. Goods-producing industries had a growth rate that year two-thirds higher than the average for the previous four years. Since both these sectors are dominated by big employers, this reduced the share of small firms in total job creation to 67%.

Does this mean that small business has had its run? It is not possible to know with any certainty yet, but it is unlikely. It appears that job creation may slow down in the coming decade and small firms will retain their share of job creation, even if the pie is smaller. Slower venture formation, higher failure rates and the slowdown in the number of people becoming self-employed will all contribute to slower growth in employment in small firms. But large organizations have already reversed their performance of 1988, which was a year of extraordinarily strong employment growth, particularly in the funded sector.

The shift out of goods-producing industries

Since the beginning of this century, there has been a steady and decisive switch away from goods-producing industries into service industries. As recently as 1931, about 30% of the Canadian population lived on farms; by 1986, that had dropped to 4%, and agriculture provided employment to only 0.7% of the labour force. Since the 1930s, governments and their agencies have dramatically increased their share of the country's economic output, until, by 1987, they employed almost a quarter of the labour force. And other services in the market sector have grown strongly: financial services have doubled their employment to 7%, a performance matched only by personal and business services, which now employ 17% of the Canadian labour force, compared to less than 10% in 1961. The stellar industry, for several years now, has been services to business management,

which employed more than 6% of the Canadian labour force in 1987, compared to 1.5% in 1961.

Small firms in market services enjoyed the most impressive growth of all the sectors - 80% over the decade - while big firms in market services barely grew at all, eking out only 5%. The only industry where big firms in market services showed much growth was services to business, in which the jobs created by big firms accounted for 99.4% of the jobs created by big firms in all market services during 1978-88.

The action is in industries dominated by small firms

There are 51 sub-industries in the economy, which can be separated into those in which the small firms employ more or less than 50% of the total workforce. If more than 50% of the total employment in an industry is in small firms, that sub-industry is defined as small-firm dominated. Of the 51 sub-industries, 19 (or 37%) were found to have more than half their 1987 employment in small firms. Between them, they employed 5.3 million people, or 47% of the total labour force. Obviously, the funded sector is dominated almost entirely by large organizations and the goods-producing sector is heavily weighted toward big firms. Trade and market services are the sectors where small firms are most dominant.

When the growth rates for all firms, big and small, are examined, the small-firm dominated half of the economy grew 45% over the decade, compared to 18% in the big-firm dominated part. Big firms grow more quickly in industries where small firms dominate (12.5% compared to 7% in big-firm dominated industries), while small firms grow more quickly in big-firm dominated industries (83% compared to 69% in small-firm dominated industries).

Ontario's place in Canadian employment

Ontario's employment patterns are quite different from those in the rest of Canada:

- Ontario has, proportionally, five times as many big organizations as the rest of Canada - 0.5% of firms compared to 0.1%.
- Ontario has a stronger presence in manufacturing, which accounts for 7.7% of its firms, compared to 5.6% in the rest of Canada.
- In the market sector as a whole, small firms employ almost half the total labour force in the rest of Canada, compared to Ontario's 40%.
- Ontario accounted for half of all the new jobs created in Canada between 1978 and 1988, although its share of the labour force in 1987

was only 41%. The province's better performance rests principally on the goods-producing sector, particularly manufacturing. Almost 18% of the new jobs created between 1978 and 1988 in Ontario were in the goods-producing sector, compared to 8½% in the rest of the country.

- Ontario's growth in the goods-producing and funded sectors is significantly higher than elsewhere - 21% and 48% respectively, compared to 8% and 29% in the rest of Canada.
- In small firms, Ontario's growth rate for all industries was 90.5%, compared to 63% in the rest of Canada.
- Small firms in personal and business services accounted for almost a fifth of all new jobs in Ontario, although they employed only 7.5% of the province's labour force in 1978. In the rest of Canada, the small firms in this sector accounted for more than a quarter of all employment gains, on a base of 8.2% of the labour force in 1978.
- Small manufacturing firms in Ontario accounted for 12% of all new jobs, although they employed 5.4% of the labour force in 1978.

Wages and salaries

Average salaries in the rest of Canada were about 88% of Ontario's in 1987, with the greatest disparities in the goods-producing industries (85%) and market services (86%). In funded services, salaries in the rest of Canada were 93% of Ontario's.

The smallest firms, employing fewer than five people, pay their employees about 40% of the salaries offered by firms with more than 500 employees. Firms with fewer than 20 employees pay at about 60% of the rate in the big firms. Average salaries in big firms in the goods-producing sector are the highest of all, at $30,194, or 20% higher than $25,848 in funded services and $24,727 in market services. Small firms generate 31% of the payroll in the goods-producing sector with 41% of the employees. Surprisingly, the imbalance is just as severe in market services, where small firms account for 34% of the payroll with 47% of the employees.

PART II

Perspectives on Entrepreneurs

Family-owned businesses

In 1987, there were about 167,000 Canadian-controlled private corporations (CCPCs) in Ontario and 70% of them were family-owned - 43% in services, 29% in trade and 27% in goods-producing industries.

Family-owned firms appear to be more effective in running their businesses. They have about 70% of the number of firms and of total sales, yet they have a larger share of equity (76%) and profits (77%) on a base of 65% of the assets. Family owned firms are less leveraged than the others and they earn a higher return on their assets.

Among the other conclusions reached by the survey:

- Family-owned firms grew at an average annual rate of 13.1% between 1984 and 1987, compared to 9.4% for non-family owned businesses. The average for all CCPCs was 12.3% a year.
- 57% are first-generation businesses. Only 8% were in the third generation or more.
- Only 12% of the sample thought that succession was a challenge for their businesses. 40% of the respondents did not know if succession was a problem and, of the 60% who did know, more than half thought it would not be a problem for at least 10 years.

Franco-Ontarian entrepreneurs

The sample used in this study may have an unusual concentration of well-established firms: they have been operating for 16 years, compared to nine for all firms in the province; their average sales are more than four times as big and their startup investment was generally higher.

Other conclusions drawn from the study include:

- Only 8% of the firms export their products or services and 71% of these firms concentrate on the U.S. The next most important destination for exports is France, with 7%.
- The average time at school is 12 years - a tenth with less than grade 9 and a quarter with a university education. For all entrepreneurs, an average of 15% have less than grade 9 and 20% have a degree.

French is used as the working language by slightly more than half the companies in this study, weighted somewhat toward internal communications with employees. The main reason why these French-speaking entrepreneurs do not use their own language more in the workplace is "out

of respect for Anglophone clientele," a reason cited by almost 40% of the respondents.

Early-stage financing

In 1988 and 1989, about $75 million was invested by private and public venture-capital funds in early-stage financings. However, 24 Canadian investing groups (about half of the firms who made early-stage investments during this period) left the early-stage financing market between 1986 and 1989, resulting in a decrease in private financings over the period. The gap was filled by public sector funds, which increased their share of the market from 21.5% in 1986 to 66.8% in 1989. Much of the growth in public-sector venture capital was in Quebec and Alberta. The latter accounted for almost half of all public-sector financings of early-stage companies in 1986-89. Ontario accounted for only 19%.

Ontario also receives less than its proportional share of early-stage financings, with only 26% of the total. In the country as a whole, the estimated amount of capital available among formal venture-capital firms that invest in early-stage companies is about $600 million. However, this money is not being invested to a great extent in the early stage companies. The private-sector venture capitalists redirected much of their attention to U.S. ventures, which attracted 23% of the funds committed by the private-sector funds during the period 1986-89.

Informal investors

Informal investors have significant amounts of capital, which they invest consistently, year after year. They invest in all regions, and, because they are builders of businesses themselves, are able to provide management assistance, the critical element of successful venture investing. Almost half already knew the management of the firm in which they were investing when they negotiated the deal. Only 6% of them found the entrepreneur through one of the match-making services. Most important, from the entrepreneurs' point of view, these investors generally did not want a control position: only 10% had a controlling interest and almost half (46%) took less than 25% of the equity.

Early-stage investments are generally smaller than expansion financing. The average investment in early-stage financings was $137,000, compared to $444,000 for expansions and $190,000 for turnarounds. The average investment was slightly more than $200,000 for the informal investors,

compared to $1.1 million for all deals in the formal venture capital industry in the private sector.

Canadian and U.S. venture capitalists invest roughly the same proportion of their funds in early-stage financings - about 25% - but only 17% of the deals and 4% of the accompanying dollars went to seed companies in Canada, compared to 45% of the deals and 28% of the dollars in the U.S. The major difficulty for Canadian venture capitalists is that they simply do not have as much confidence in the management capabilities of Canadian entrepreneurs - and quality of the management is the single most important factor in the investment decision.

PART III

The role of government

In its new plan, designed for 1990-95, Small Business Ontario (SBO) has developed an ambitious vision for the contribution it can make to the province's entrepreneurs, current and future. The goals comprising this vision include:

- An Ontario sympathetic to the entrepreneurial ethic, valuing innovation, self-reliance and calculated risk-taking.
- A growing number of Ontario entrepreneurs owning and operating their own businesses or applying their talents within larger organizations.
- Greater numbers of small businesses entering export markets.
- An education system that fosters the entrepreneurial ethic among our young people.
- A province-wide information network providing relevant bottom-line intelligence to both startup and established entrepreneurs.
- An active private sector involved and committed to supporting the growth of entrepreneurship through independent or joint public-private initiatives.
- Government at all levels sympathetic and responsive to the need to maintain a public policy environment conducive to entrepreneurship.
- A widely recognized Small Business Ontario generating interest and support in both the private and public sectors.

By the end of 1990, Small Business Ontario had 26 Self-Help Offices established around the province. Most of them (22) are run jointly with the municipality in whose offices they are located. There are also about 100 kiosks in smaller communities too small to support a full Self-Help Office.

The 1988 report of the Premier's Council found that lack of equity capital was identified as a constraint to growth by 74% of the firms its researchers interviewed. Programs which exist to meet this need include: *New Ventures*, for entrepreneurs who do not have the necessary collateral for commercial loans; *Ontario Development Corp. (ODC)*, and Northern ODC and Eastern ODC, which makes loans and loan guarantees to secondary industries, exporters and tourist operators; *The Federal Business Development Bank*, which provides financial assistance in the form of loans, loan guarantees and equity investments; *Innovation Ontario Corporation*, which provides equity and quasi-equity capital to technology-based firms in the early stages of development.

Also, SBO includes *Youth Startup Capital*, which has three principal objectives: to develop and encourage entrepreneurial activity among young people in Ontario, to provide access to business financing not normally available to young people, and to assist in the development of entrepreneurial skills.

Other activities of SBO include supplier development, monitoring the effects of pay-equity legislation and payroll taxes. The 1990 budget contained several measures aimed at assisting small businesses, including significant concessions to small firms in connection with the collection of the Retail Sales Tax.

Entrepreneurship in education

In the spring of 1990, the Ministry of Education introduced its Entrepreneurship Studies program for students in grades 11 and 12. To complement this initiative, Small Business Ontario designed a program for students in grades 7 and 8, called Visions. It aims to introduce them to the concept of entrepreneurship, to enable them to recognize the benefits that entrepreneurship can bring to our society and to encourage them to consider entrepreneurship as a viable career possibility.It is anticipated that Visions will be available to all schools in the province in 1992.

The Entrepreneurship Studies program prepared by Ontario's Ministry of Education is designed to nurture a spirit of innovation in students. It is specifically not aimed at teaching students how to start a new business, nor is it intended to be an extension of courses in business administration. Rather it seeks to provide students with opportunities to discover that entrepreneurial activities demand vision, a high degree of initiative and skill and that these activities can be in non-commercial as well as commercial

ventures. The aims of the program include: providing students with opportunities to assess their interest in and aptitude for entrepreneurial activities; recognizing that entrepreneurial skills and behaviours can be developed; and using the process of self-assessment and goal-setting to set personal goals and achieve them.

People and skills

Five years ago, about 62% of the employees in Ontario's auto parts industry were unskilled. Today, 33% in that industry are unskilled. More than half the new jobs in Canada now require a grade 12 education or better; in another decade, this qualification will be adequate for only 37% of new jobs. Yet one third of Ontario's students drop out of school before they receive their diploma.

According to the Premier's Council, industry spending in Canada on employee training is half the spending in the U.S., and a quarter that of Germany's. Ontario's Ministry of Skills Development spends about $280 million a year on training. Small firms give a high rating to the services offered by the Ontario Skills Development Offices (OSDOs). During 1989-90, this program assisted 13,000 clients, 94% of them with fewer than 200 employees.

There is also a lack of expertise in small firms in personnel management, a dearth that is exaggerated because many business owners do not appreciate the extent to which they need help. To address this need, Small Business Ontario mounted a pilot project in the spring of 1990 to offer three workshops on people management to business owners. The workshops attempted to demonstrate that people management lies at the heart of any solution to competitiveness and that owners can control their futures in this regard through proven techniques.

The Technical Personnel Program was introduced in 1989. It is designed to raise the level of technical skills in smaller Ontario companies, to promote capital investment and accelerate the adoption of new technology and to reduce manufacturing costs, increase productivity and improve export capability. In its first year, TPP approved 206 applications (82%) for an average contribution of $33,000 on an average salary of $44,000.TPP commitments in its first year exceeded $5 million. Participating companies that were doing Research & Development committed almost $100,000 in R&D funds over three years.

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Part I

Small Business in Ontario's Economy

A review of the economic environment in which small businesses operate and an assessment of the contribution they have made to job creation since 1978. Also, the impact of the decline or growth in employment in large organizations.

CHAPTER 1
THE ECONOMIC ENVIRONMENT

The decade of the 1980s witnessed the emergence of small business from obscurity into public consciousness. This new-found, still sceptical, respect for small businesses is based, of course, on their demonstrated ability to create new jobs at a time when large firms are shedding labour. The phenomenon first surfaced when small-business employment held firm through the jarring adjustment of the 1981-82 recession, the steepest since the Great Depression of the 1930s. And respect blossomed throughout the boom of 1983-89, the longest sustained economic expansion since World War II, during which small firms accounted for the bulk of new jobs.

The new decade of the 1990s offers as much, if not more, jarring adjustment, but no-one, least of all small business owners, can predict who will benefit most this time around. The decade started unpromisingly, under a threatening cloud of high interest rates and an overvalued Canadian dollar, but the outcome of the decade will rest on more profound trends. In Canada, as in every developed country, the economies that prosper will be those that provide a supportive environment for innovation and adaptation. The outcome for small firms rests on two huge challenges: the degree to which they can maintain their advantage over big firms in providing such an environment for their employees, suppliers and customers; and their success in improving their financial management and their marketing to cope with a progressively tougher and more volatile marketplace. Big firms have already demonstrated their skill in assembling ever-larger pools of financial and marketing clout but they have yet to develop techniques for making large human systems flexible and sensitive enough to individual needs and wants to consistently nourish innovation and adaptation.

For Ontario, the decade started ominously. After leading the country in every economic indicator during the 1980s, it tripped in the second quarter of 1990, falling into a recession that threatened to be more severe than in any other province in Canada. The underpinnings of the province's extraordinary success in the past decade are now retrenching. Yet the province has built a powerful and resilient industrial infrastructure that is capable of adapting to the pressures of global competition and whirlwind social trends. This chapter attempts to take stock of the environment for small firms in the 1990s by reviewing developments of the past decade

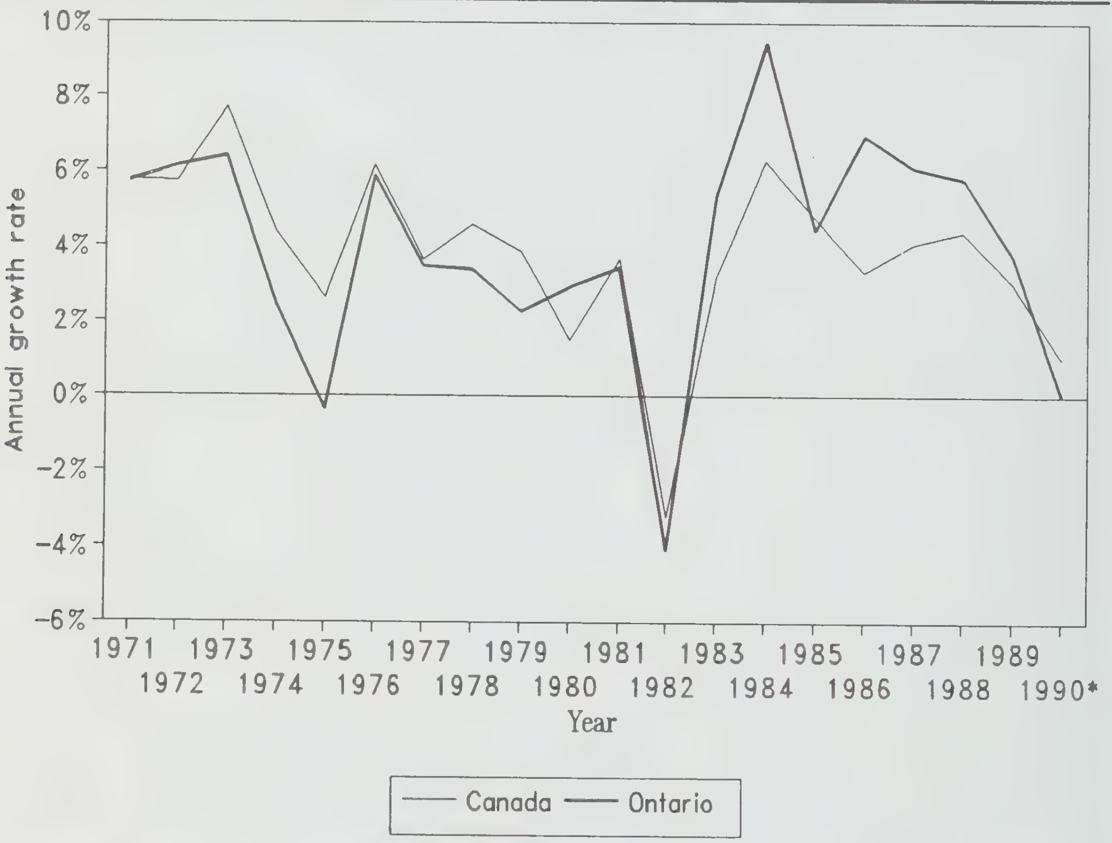
across a broad range of economic indicators. It will show how entrepreneurship has prospered and how it is threatened now by high interest rates and an overvalued Canadian dollar.

The growth decade

In the 1980s, Canada enjoyed the second fastest economic growth of all the major developed countries, surpassed only by Japan. As Chart 1.1 shows, Ontario was the engine of this growth, with annual increases in Gross Domestic Product well ahead of Canada's.

Chart 1.1[1]
Ontario lagged in the 1970s and soared in the 1980s

Annual growth in Gross Domestic Product for Ontario and Canada, 1971-90



****Estimate on the basis of GDP growth in the first half.***

[1]Source: *Bank of Canada Review*

Since Ontario represents 40% of the national economy, this means that Ontario performed significantly better than the other provinces during the 1980s. The 1970s were a different story, as the chart shows, because Ontario lagged the other provinces for all but two of the 12 years between 1971 to 1982. Overall, however, Ontario still came out ahead of the national average for the two decades, as Table 1.1 shows, thanks to a remarkable seven years after the last recession, when growth averaged 6% a year; this was better than any of the Big Seven industrialized countries.

Table 1.1[2]
Two decades in the growth stakes, Ontario and Canada

Average annual growth rate of real Gross Domestic Product		
Period	**Canada**	**Ontario**
	%	%
1971-82	3.8	3.1
1983-89	4.1	6.0
1971-89	**3.9**	**4.1**

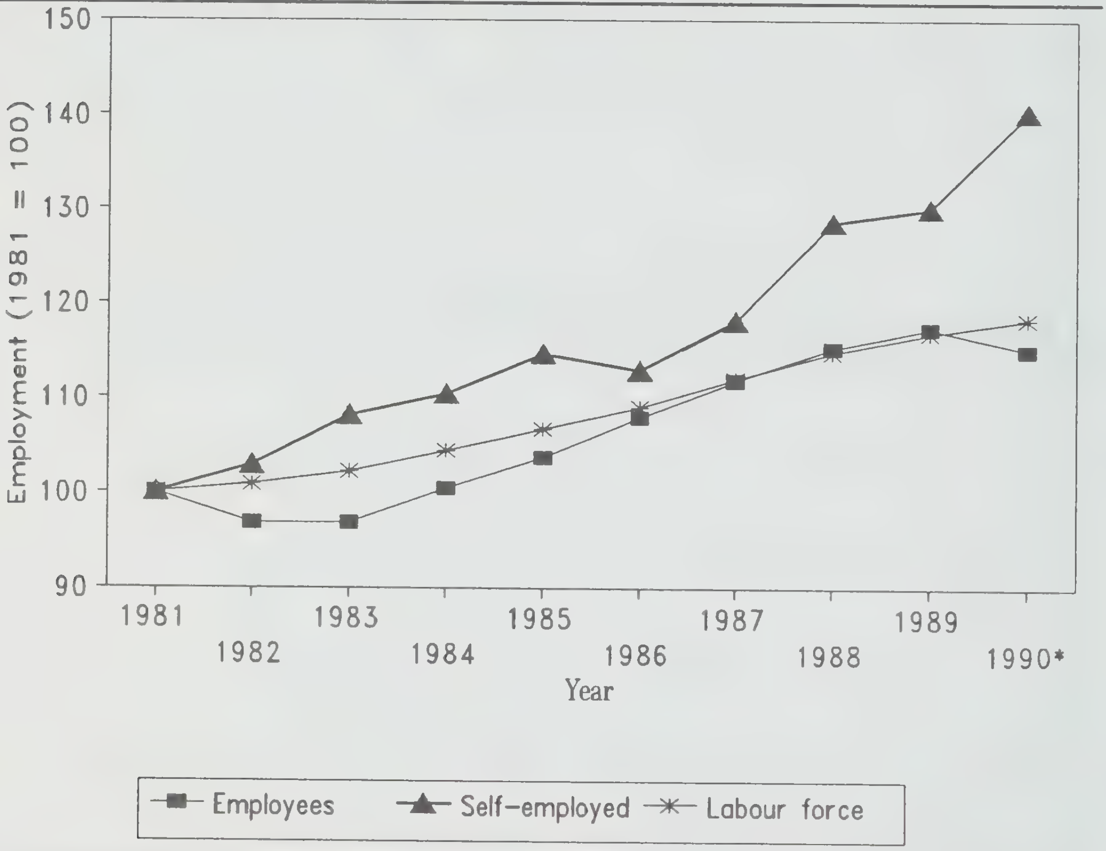
The gains of this impressive performance are now in danger of being reversed. As this report went to press, Ontario could hope for little better than zero growth in 1990, while the other provinces enjoyed the prospect of at least some growth. Ontario has been hit hard by severe setbacks in manufacturing industries and in real estate, which accounted for so much of the gains during the 1980s.

The growth record of the past decade was built largely on the rapid increase in the labour force (the alternative source of economic growth, productivity, has not been a stellar performer). As Chart 1.2 shows, the province's record of job creation has been impressive. Although the number of employees dipped during the 1981-82 recession, as might have been expected, employment recovered strongly during the balance of the decade, finishing up 17% ahead of 1981, edging out the growth rate of the labour force as a whole. Unemployment in 1989, at the decade's end, was accordingly substantially lower at 5.5%, compared to 7.7% for Canada. 1990, however, saw some of those gains taken away, as the chart shows.

[2]Source: Ibid. *Bank of Canada Review*

Chart 1.2[3]
Ontario's labour force in the 1980s

Growth during 1981-1990 of Ontario's labour force, number of employees and number of self-employed people (incorporated and unincorporated). 1981=100.



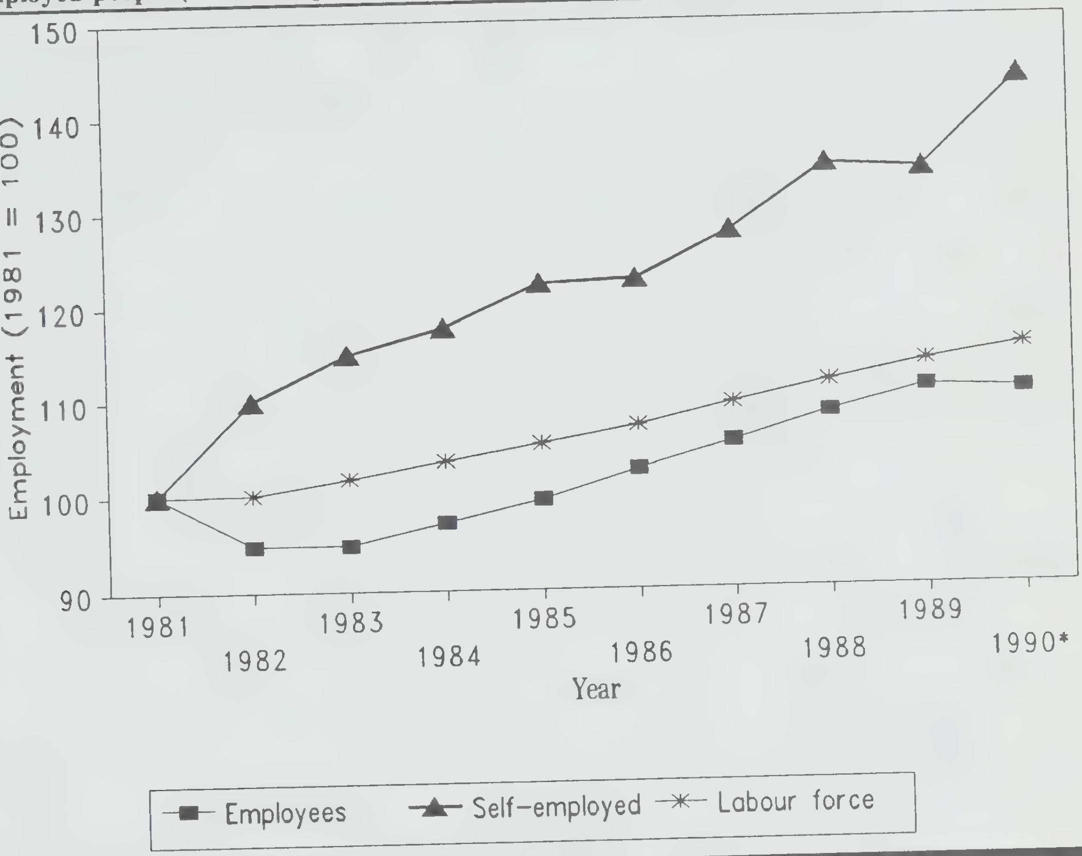
**Note: Statistics for 1990 are estimates based on results to July.*

The pattern was similar in Canada as a whole, but there were some important differences. As Chart 1.3 shows, the dip in employment during the 1981-82 recession was bigger in Canada than in Ontario, the subsequent recovery was less spectacular, and the decline in 1990 is expected to be less severe.

[3]Source: Statistics Canada, *The Labour Force*

Chart 1.3[4]
Canada's labour force in the 1980s

Growth during 1981-1990 of Canada's labour force, number of employees and number of self-employed people (both incorporated and unincorporated). 1981=100.



**Note: Statistics for 1990 are estimates based on results to July.*

The most spectacular part of these charts, however, is the progression in the number of self-employed people in both jurisdictions. Over the ten years to 1990, self-employment grew 44% in Canada and 40% in Ontario, while the number of employees grew 10% and 15% respectively. The self-employed now represent about one in seven of the people employed in both jurisdictions.

The patterns of growth in self-employment are also quite different in the two jurisdictions. In 1982, the number of employees fell more sharply and the number of self-employed people jumped more sharply in Canada

[4]Source: Ibid. *The Labour Force*

than in Ontario. This suggests that the sharper the cutback in employment is, the stronger is the growth in the ranks of the self-employed. This is consistent with a significant body of research which has found that many entrepreneurs are pushed by economic misfortune into starting their first venture. In a severe recession, many people who have been thinking of starting their own businesses are pushed into it sooner than they had anticipated.

A surge like this inevitably breeds a subsequent reaction, which duly came in 1986. The economy was booming and there were jobs galore in the big companies, which were by then rehiring some of the people they had let go earlier. In Ontario, the number of self-employed people actually declined in 1986, presumably in response to the enormous demand for skilled people in the fourth year of the boom. The same pattern appeared in Canada as a whole, but in a less exaggerated form; the growth of self-employment flattened rather than declined in 1986. There was a similar pause for breath in 1989, before a dramatic resumption in 1990, when it appears that the 1982 phenomenon was repeated: self-employment grew strongly while the number of employees declined in Ontario and stagnated in Canada.

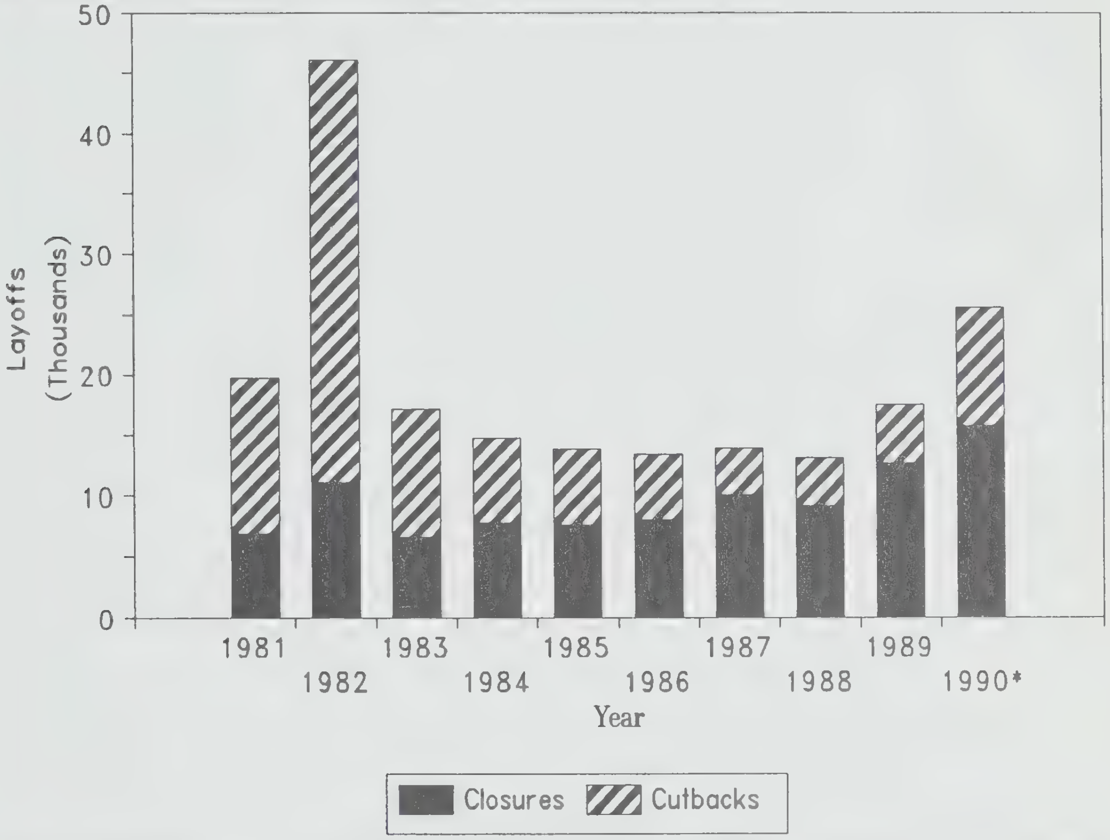
The 1990 recession

At the time this book went to press, it was still too early to predict the severity of the dip in employment in the current recession. Forecasts as to the severity of the recession varied from "short and shallow" to "much worse than 1981-82". In the fall of 1990, however, there were already signs that this recession was starting to bite hard and that the economic environment was more fragile than it was in 1981. In Ontario, permanent and indefinite layoffs involving more than 50 employees had still not reached the level of 1982, as Chart 1.4 shows, but they had grown strongly in 1989 and 1990. By September, actual and announced layoffs for 1990 had reached more than 25,000, compared to about 46,000 in 1982. Disturbingly, however, the layoffs in 1990 had a much higher component of permanent closures of plants or portions of plants. These layoffs are jobs that are lost forever, because no plant exists to which workers can return when the next boom starts. In 1982, these layoffs represented only one quarter of the total. Three quarters were general cutbacks to correct excess inventory or to remove the serious surplus labour that had built up in the corporate sector in the 1970s. The proportion of layoffs classed as general cutbacks was nearly halved in 1990, when general cutbacks accounted for

less than 40% of the total. More jobs had been lost by September, 1990, from complete cessations of activities in companies or divisions, than had been lost for the same reason in all of 1982.

Chart 1.4[5]
Big-business layoffs are rising again in Ontario

Permanent and indefinite layoffs involving 50 or more employees, by closure of operations and by general cutbacks of continuing operations in Ontario.



**Note: The figures for 1990 include announcements up to September. They include layoffs announced for 1990 but not yet implemented.*

It seems that the normal business cycle entails excess recruitment shortly before the peak of an economic upswing and an inevitable correction when the recession starts to bite. One of the reasons for the large number of layoffs in 1982 was that Canadian businesses were unusually bloated in

[5]Source: Ontario Ministry of Labour

their assets and their employment. The country was barely touched by the mid-1970s recession that was set off by the jump in oil prices. As a result, businesses went more than 10 years without a significant correction, which made the correction that much worse when it came. The situation is quite different in 1990, because there is far less fat in the system. Bankers and others familiar with corporate balance sheets say that inventory control has improved by several orders of magnitude since 1981. This means the layoff figures are a more sensitive measure of current conditions than they used to be; they are not as big and they swing less violently. Formerly, employers delayed impending layoffs for several months in the hope they wouldn't be necessary, until the resulting build-up of inventories became so large that everyone realized at the same time they could not ride out the recession without layoffs and they all acted simultaneously. Better inventory control avoids this "bunching". Manufacturers still miscalculated this time, however, because they had run out of production capacity in the late 1980s and chose to expand strongly in 1988, embarking on a mini hiring boom that had to be reversed as soon as the economy slowed in 1990. Notwithstanding this misjudgment, there is still cause for concern at the high level of layoffs, since they contain a higher proportion of core jobs than the bigger layoff numbers of 1982.

The layoffs should not, however, be viewed in isolation. Part of what is happening is a radical restructuring of industry everywhere in the world and Canada is no exception. Products which can be produced just as effectively in low-wage countries are being manufactured there now, not in North America, Europe or Japan. The developed countries are compensating by creating new niches for themselves that depend on the greater sophistication of their labour forces. This part of the equation is less well-observed because many of the new jobs in the new niches are in smaller firms or in smaller numbers, so they are not reported to governments and the press doesn't notice them. The critical question is whether manufacturers in Ontario, with half of all Canadian manufacturing, are in tune with this global trend. Certainly, small manufacturing firms have been astonishingly effective in creating employment in the past decade, even as the big manufacturers were shedding labour very rapidly (see Chapters 2 and 3).

It is too soon to judge how Ontario is doing in the race to keep pace with the global restructuring, although this recession will probably deliver answers to this question sooner than expected. There is, however, immediate concern over the financial resilience of the corporate sector in

Canada. A recession brings to the surface all kinds of problems that have been hidden during the boom years; the big issue in this recession is Canada's and Ontario's ability to compete in the U.S. and elsewhere when debt loads are at historical peaks and interest rates and the Canadian dollar are both too high for comfort. This encompasses much more than the Canada-U.S. Free Trade Agreement, which is a focus for but by no means the heart of this country's challenge to be globally competitive.

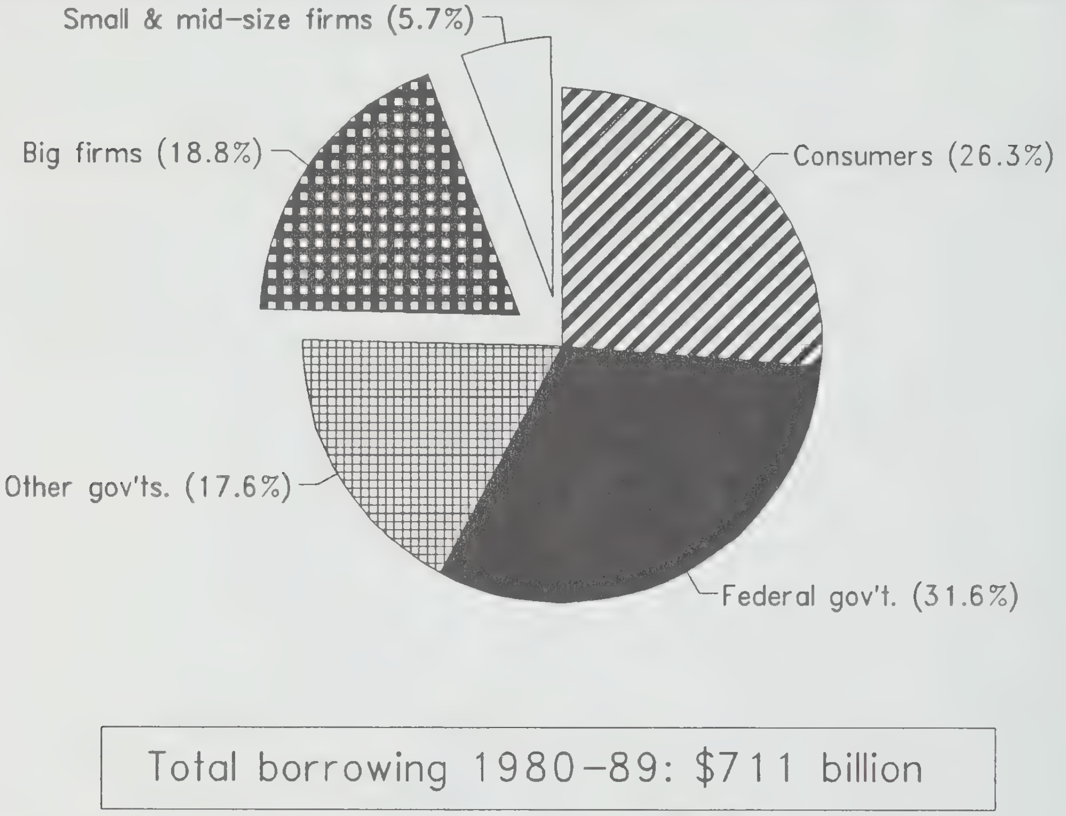
The financial resilience of Canadian businesses

Companies, consumers and governments all have a great deal less room to manoeuvre going into the 1990 recession than they did going into the 1981-82 recession. This severely limits their ability to help each other through this recession. Consumers have borrowed at unprecedented rates. In the six years from 1983 to 1989, consumer debt doubled and residential mortgages increased even faster, ending the decade 117% higher than the total in 1979. These increases easily surpass the increases over the same period of Gross Domestic Product (60%) and wages and salaries (62%). This means that, in this recession, cuts in income will translate more quickly into cuts in demand, because consumers are less able to borrow to tide themselves over until their income rises once more. As this book went to press, retail sales figures for the fall were not in, but susceptible retailers (non-essential items like cars and other durable goods) had been reporting sales declines of up to 10% (before adjusting for inflation) since April and May.

The position is even more parlous for governments, which borrowed so extensively in the 1980s that they, too, would risk the displeasure of their creditors if they were to allow budget deficits to soar much higher. With a deficit more than one-fifth of its total expenditures, the federal government simply cannot spend its way out of a recession, particularly when interest charges are already eating up one third of its revenues. The same is true for the provincial and municipal governments, which have borrowed only slightly less enthusiastically, as Chart 1.5 shows.

Chart 1.5[6]
The borrowing binge in the 1980s

Net borrowing by major consumers, business and governments, Canada, 1980-89



Notes: Borrowing for small and mid-sized companies is assumed to be entirely from the banks. Net sales of corporate bonds, commercial paper and bankers' acceptances are assumed to be entirely for big businesses. Borrowings by governments include bonds and Treasury bills only. Borrowing by consumers includes residential mortgages and consumer credit.

With total borrowing by consumers, corporations and governments at $711 billion during the 1980s, Canada has little room to manoeuvre in the 1990s. At a time when international financial markets are becoming less friendly toward North American deficit financing, governments' ability to borrow at reasonable rates of interest depends to a large degree on whether the U.S. federal government can reduce its demands on the international financial market. A significant increase in government debt requirements would seriously harm the ability of the private sector to raise funds. It

[6]Source: Ibid. *Bank of Canada Review*

could also cause interest rates to remain at the high levels of recent years, endangering still further the ability of small firms, in particular, to survive. Yet the pressure to increase spending in all three levels of government will mount rapidly during this recession, presenting them with difficult choices in setting priorities.

Small and mid-sized firms were the only players in the economy that avoided the temptation of rushing to acquire more debt in the 1980s, accounting for only $41 billion of the $711 billion borrowed during the decade. They relied almost exclusively on banks for their debt, unlike big businesses which did not expand their bank loans much, preferring to "securitize" their debt by issuing large amounts of corporate bonds and short-term commercial paper. [This may explain the banks' decisions to acquire ownership of the investment houses that handle bond issues.] Corporate bonds are, of course, immune from sharp shifts in interest rates because their rates are fixed, so big firms are probably less vulnerable to a rise in interest rates than they were a decade ago. However, they are still vulnerable when profits drop, because their high leverage entails commitments to pay large interest charges.

In 1989, corporate profits (which are dominated by big firms) were only 57% higher than in 1981, while big-company debt was up 140%, as Chart 1.6 shows. This means that big firms are now carrying 50% more debt than they carried the year before the last recession for each dollar of profit. Small firms, by contrast increased their debt load only 50% during the decade. Precise measures of small-business profits are not available, but a good indication is what happened with unincorporated businesses, almost all of which are small. Net income from unincorporated businesses was up 153%[7] during the 1980s, while outstanding debt rose 33%. This means that, compared to 1981, small, unincorporated firms are now carrying about half the debt they carried in 1981 for each dollar of profit.

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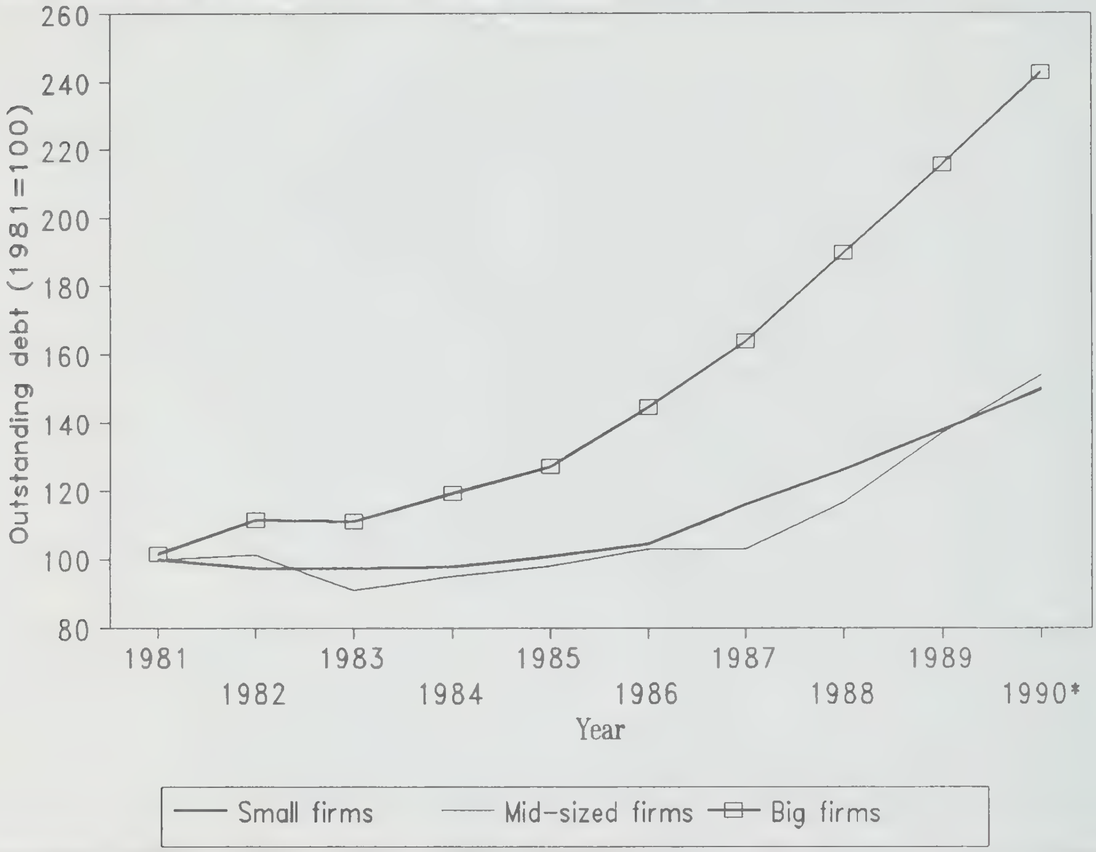
[7]Source: *Bank of Canada Review*

Chart 1.6[8]

Big firms have taken on lots of debt since 1981

Net borrowing by big, small and mid-sized firms. 1981=100, Canada, 1981-90



**Estimate*

Notes: Bank debt is allocated by firm size assuming small firms borrow under authorized limits to $5 million; mid-sized firms go to $25 million and big firms more than $25 million. See notes to previous table for methodology in calculating debt levels.

Although small firms are the only players in the economy to have improved their relative debt position, they are still always vulnerable to high interest rates, because profit margins are so much tighter than they are in big firms. With businesses, governments and consumers now all vulnerable to high interest rates, the rise in interest rates in the spring of 1990 had an immediate and sharp effect. Consumers quickly trimmed their retail spending and vacated the housing market. The reaction from governments took a little longer, because the revenue losses from lower

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[8]Source: Ibid. *Bank of Canada Review*

incomes take longer to materialize. Banks, still smarting from their sloppy lending practices of the last recession, have put their potential problem loans under a microscope very quickly, extricating themselves from positions in which they felt uncomfortable. This invariably affects small firms more than big firms. In a survey conducted in June, 1990, the Canadian Federation of Independent Business found that 34% of its members said their bankers had changed their credit arrangements in the previous six months. About half of these cases were reductions in the availability of credit and just less than a third were changes to the conditions of existing loans.

In this environment, there is real concern that the monetary policy pursued by the Bank of Canada for most of 1990 may have put undue pressure on all the major borrowers. Interest rates in 1990 were still far from the stratospheric levels of 1981, when the prime rate reached 22¾%, but so was the inflation rate, which was less than 5% in 1990, compared to more than 12% throughout 1981. The real prime rate (prime rate less the inflation rate) in 1990 has been running at levels comparable to those of 1981, and for longer, as Chart 1.7 shows.

The level of real interest rates is important to the balance sheets of firms, because the value of the assets that provide collateral for debt increase at a slower rate than the interest on the debt. In 1987, the Canadian Federation of Independent Business surveyed its members' attitudes toward banks and found that collateral requirements were the biggest concern for 30% of the survey respondents[9]. Collateral requirements averaged 3.3 times the credit limit of firms in Ontario, 2.2 times the limit in the rest of Canada. High real interest rates over a period of years therefore erodes the solidity of corporate balance sheets, restricting their ability to borrow further. The impact is even bleaker now than it appeared to be in 1989, because much of the borrowing power used up during the 1980s was built on the strength of real estate assets, which have declined significantly in value in the past year or so, pushing real interest rates up still further.

Since the 1970s, real interest rates have steadily gone higher and higher. In that decade, real interest rates averaged 1.2%, including one year when the real rate was negative. In 1981, real prime rate averaged 7%,

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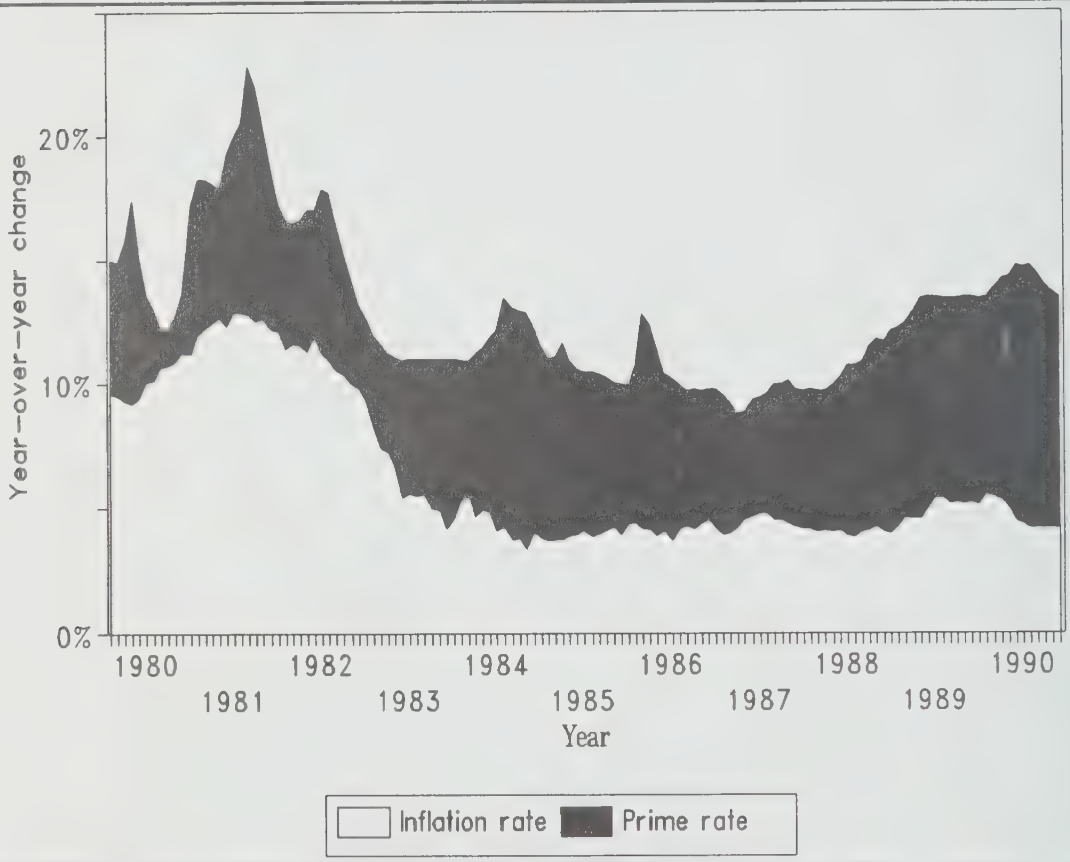
[9]Source: *Small Business Views the Banks: The Bottom Line*, prepared for the Canadian Federation of Independent Business by M.J Grant & Co. 1988.

rising above 8% for 12 weeks of the year. In the eight years following May, 1982 (when interest rates came down to more tolerable levels), real prime rate stayed above 5% for all but 20 weeks, averaging 6.7% over the period. In 1990, real prime did not go below 8% for the first 10 months at all, averaging 9%. In the long-term, over many decades, real interest rates average about 3%, so it's fair to say the 1980s have been a decade of extraordinarily high real interest rates, and 1990 has been worse than 1981.

Chart 1.7[10]
Real prime rate, after inflation, is at record levels

Average monthly prime rate and year-over-year increase in the Consumers' Price Index, Canada, 1980-90. Shaded area is the real prime rate.



With restricted ability to borrow in hard times, these high interest rates make small and large businesses more vulnerable to adverse economic

[10]Source: Canadian Bankers Association, *Bank of Canada Review*

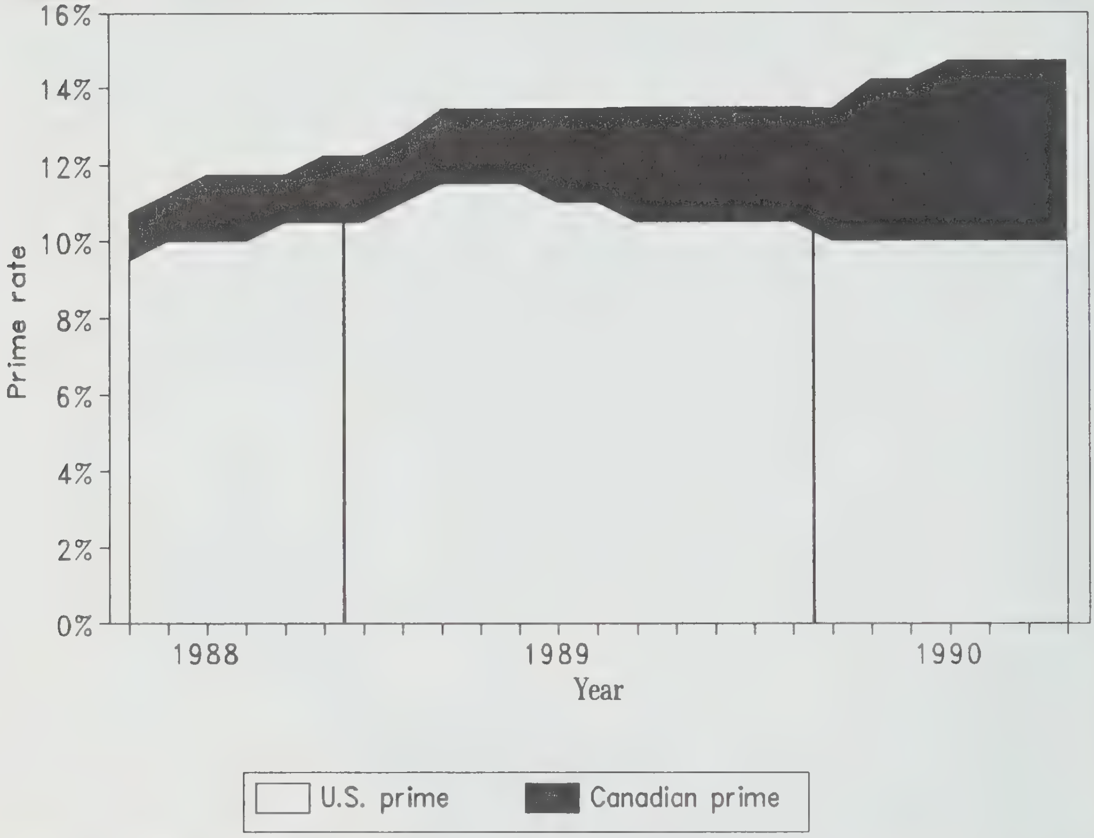
conditions. When debt levels are high, interest charges wipe out a large portion of operating profits and worsening business conditions can quickly eliminate after-interest profits. Not surprisingly, bankruptcies rose sharply in 1990, which is normal for any slowdown. Bankruptcies are only a part of overall failures, however - many entrepreneurs just close their doors and walk away, others go into receivership, with economic effects far surpassing that of bankruptcies. It appears (see Chapter 2) that overall failures started rising sharply in 1987. This is probably a reflection of prolonged high interest rates and high debt levels.

Another aspect of interest rates that is just as important as the real prime rate is the spread between Canadian and U.S. prime rates. As Chart 1.8 shows, this spread widened significantly in 1989 and 1990.

Almost 30% of Canada's economy depends on trade and more than 70% of our trade is with the U.S., so a fifth of Canada's Gross National Product depends on trade with the U.S. The comparative costs of doing business in the two countries are, therefore, critical to the success of Canada's economy. When the spread is as wide as it was in 1990, this poses serious problems for Canadian businesses. [Japanese interest rates are significantly lower than U.S. rates, so increased debt leverage poses even greater threats to both countries in competing with Japanese firms.]

Chart 1.8[11]
The spread between U.S. and Canadian prime rates

Prime rate charged to the banks' best customers in Canada and the U.S. (shaded area is the spread). 1988-90



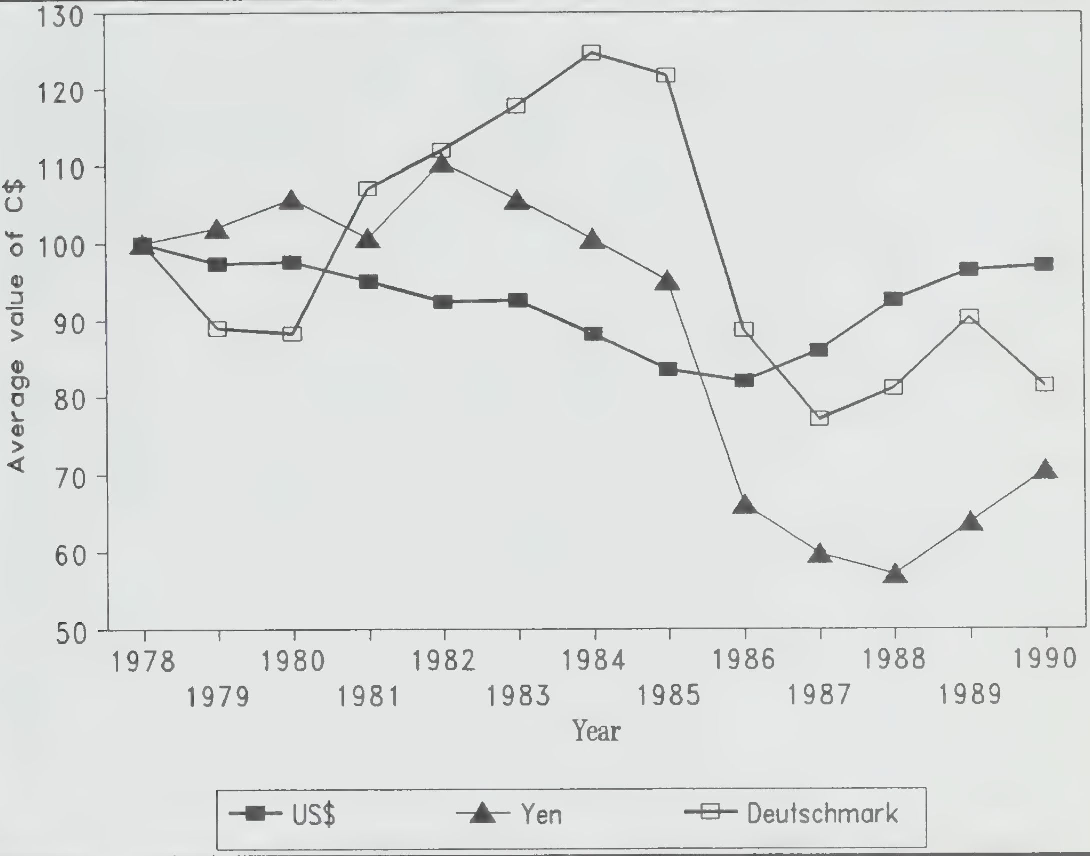
Added to this trading disadvantage is the appreciation of the Canadian dollar against the American dollar in the period from 1986 to the first half of 1990, as shown by Chart 1.9.

[During this period, the Canadian dollar was declining against other major currencies, reflecting the weakness of the American dollar. The soaring Canadian dollar in the mid-1980s was also a reflection of the American dollar, which was very strong then. However, the impact on Canada of a rising foreign exchange rate is far more significant against the US dollar than against other currencies.]

[11]Source: *Bank of Canada Review*

Chart 1.9
The Canadian dollar's roller-coaster ride

Number of units of major foreign currencies required to buy C$1. Annual averages, 1978 = 100.



After 1986, the C$ rose from a low of 69¢ (US) to a peak of more than 87¢, before it began to decline. When the Canadian dollar is worth 87¢ in the U.S., Canadian manufacturers find it tough to compete with American manufacturers. For some, particularly in the resource sector, where prices are set internationally in American dollars, it has meant significant declines in profit margins. For others, it has become difficult, sometimes extremely so, to match American prices both in their markets and in domestic markets. Inevitably, this has resulted in lost business and layoffs.

In summary, the prolonged period of high real interest rates, the overvalued Canadian dollar between 1986 and 1990, and the huge increase in the debt leverage of big businesses, governments and consumers have combined to make small firms vulnerable to an adverse economic climate. Fortunately, small firms have kept their own debt leverage under tight

control, equipping them to deal with the current recession more flexibly. Continued high interest rates, however, pose enormous dangers to small firms.

Free trade

There is a great deal of debate over whether free trade is wreaking havoc with the industrial base of Canada in general, and of Ontario in particular. The rising tide of layoffs in large companies, illustrated in Chart 1.4, is often cited as "proof" that free trade is killing Ontario's manufacturing base. It is far too early to assess accurately the long-term impact of free trade, however, and there are several other potential reasons apart from free trade for the surging rate of layoffs.

There is clear evidence that big manufacturing companies hired too many people in 1988, making the 1990 layoffs inevitable as soon as the economy cooled (see Chapter 2); this slowdown, in turn, was precipitated in part by a U.S. economy running out of steam, which diminished the demand for Ontario's goods, particularly in the automotive sector. These are both normal cyclical trends which result in layoffs. At a deeper level, however, many of the layoffs are part of a continuing, massive restructuring of industrial production that began in Canada in the 1970s and has been gathering pace ever since - as it has done in all industrialized countries. And there is a growing perception in Canada that the tax environment is more welcoming in the U.S. than in Canada, so some companies are moving all or part of their operations south of the border.

The last two of these four factors are linked to the Free Trade Agreement, which was intended to expose Canada to these global changes before it is too late. A major part of the impact of the agreement is therefore psychological, since Canadian businesses know they have to adjust their operations *before* all the tariffs come off and Canadians generally have been made more aware of American buying opportunities. Free trade has therefore put pressure on Ontario's manufacturing base, although it is by no means the only pressure point. It has also probably been the spur to the creation of many industrial expansions which don't receive as much publicity as the big layoffs.

All that can be said with certainty is that the effect of the exchange rate against the US$ and the spread between interest rates in the two countries have had a far more powerful effect than free trade in the short term. When these two aberrations return to more normal levels, the effects of free trade may be seen more clearly.

Cross-border shopping

The best indication so far of the effects of free trade lie in an examination of the phenomenon of cross-border shopping. It is estimated[12] that Canadians who cross the border to shop in the U.S. may be draining up to $500 million in retail sales from domestic outlets. This is hurting local retailers in the border areas, which have a population of about 1.2 million, or 13% of Ontarians. It is also hurting the provincial government, which is losing almost $50 million in tax revenues. And the lost retail sales are also expected to reduce by more than $100 million a year the federal government's tax revenues from the Goods and Service Tax, starting in January, 1991.

In 1990, an estimated 20 million Canadians made same-day excursions across Ontario's border points by surface transportation. In the first six months of 1990, 9.9 million made these trips, an increase of 84% from the first six months of 1987. By contrast, only 6.7 million Americans crossed into Ontario on one-day trips in the first six months of 1990, a decrease of 7% from the same period in 1987. There are now three Canadians crossing into the U.S. for every two Americans crossing into Ontario; three years ago, there were three Canadians for every four Americans. This is responsible[13] for about 30% of the $1-billion increase in the province's annual tourist deficit with the U.S. between 1987 and 1989.

The Free Trade Agreement provided a major psychological boost to individual shopping sprees across the border[14]. It triggered greater consumer awareness of the price differences, which were subsequently widened to Ontario's disadvantage by the 12% appreciation of the Canadian dollar between 1986 and 1989. The major spur to shop in the U.S. came from the wide gap in the price of a single product, gasoline, which costs 16¢-21¢ per litre more in Ontario than in the adjoining border states. This comparison was done before the price of oil jumped after the crisis in the Persian gulf, which won't change the gap significantly because more than three-quarters of the price gap is accounted for by taxes. Federal and provincial taxes, which are levied in roughly equal amounts in Ontario,

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[12]Source: Internal study by the Ministry of Industry, Trade & Technology: *Cross-border shopping*, August, 1990

[13]Source: Ibid.

[14]Source: Ibid. *Cross-border shopping.*

total 23.4¢ a litre, compared with about 7.9¢ a litre in the U.S. Taxes on gasoline by both levels of government in Canada increased by about 30% in 1988. The industry initially swallowed the increase because the market was so competitive, but, as prices increased over the next year or so, drivers flocked to the U.S. Consumption in Canada's border areas decreased 13% (about 100 million litres) between 1987 and 1990, most of that coming in 1989-90. In the same period, consumption throughout the province increased 1%.

The second major target of Ontarian shoppers in the U.S. is groceries, which accounted for about 40% of the traffic[15]. Prices in the U.S. are notably lower in items such as dairy, poultry, paper and household cleaning products. It might have been expected that beer and liquor would pose major difficulties for retail sales in Ontario. The average price of a case of 24 bottles of Canadian beer is C$11.19 in U.S. border cities, compared with C$23.45 in Ontario. However, this has not been a major target for cross-border shopping, although it has probably led to more business for U.S. border restaurants and bars, both from Canadians visiting them more often and from Americans visiting us less often. Liquor sales in the border areas increased 1% in 1990 over 1989, compared to 4% in the rest of the province. Other items which are rapidly becoming more important in cross-border shopping are consumer electronics, building materials and large appliances.

The greatest concentration of cross-border shopping is in the Niagara peninsula, which accounts for 43% of the traffic. Windsor accounts for 27%, followed by Sarnia (11%), Sault Ste. Marie (11%) and Fort Frances, Cornwall and Thousand Islands/Kingston (all less than 4%). The traffic in the Niagara peninsula is drawn mainly from Toronto, Hamilton, St. Catharines, Fort Erie and Niagara Falls. A recent study[16] has reported that tax levels are a significant factor in the higher price levels in Ontario. Average federal, state/provincial and municipal taxes on small retailers in Buffalo, for example, were less than two-thirds of the taxes on comparable firms in the Toronto. Most of the gap is accounted for by municipal taxes, which are more than four times higher in Toronto. Comparable, though less dramatic, differences were found in northern Ontario, where small retailers

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[15]Source: John Winter Associates: *Committee for Fair Shopping*, March 1990

[16]Source: Canadian Federation of Independent Business, *Borderline Business: Taxation and Cross-border shopping*, October 1990.

in Duluth pay about 90% of the taxes paid by a comparable retailer in Thunder Bay.

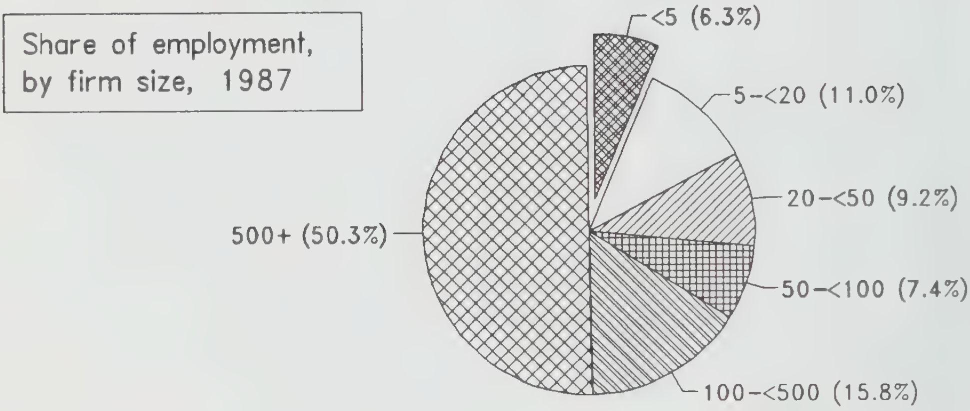
Cross-border shopping has not had a major impact on the manufacturing industry in Ontario, but it has affected the retail and tourist industries in border areas. The major short-term avenues open to governments to redress the imbalance are lower taxes for border communities and more effective collection of federal and provincial sales taxes at border crossings.

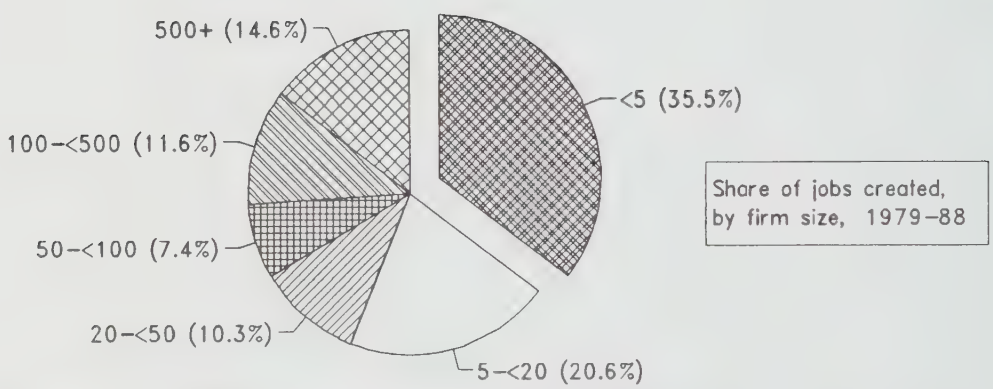
CHAPTER 2
THE ECONOMIC PERFORMANCE OF SMALL BUSINESS

In the decade between 1978 and 1988, small firms accounted for 74% of all the new jobs created in Ontario.

Chart 2.1[1]
Small firms out-perform all others in job creation

Share, for each size of firm, of total employment in Ontario in 1987 and in the total jobs created in Ontario during 1979-88





[1]Source:Unless otherwise stated, the data in Chapters 2 and 3 is based on Employment Dynamics, produced by the Small Business & Special Surveys division of Statistics Canada.

This enabled small firms, defined as those employing fewer than 100 people, to raise their share of the workforce to 34% from 31%, mostly at the expense of big employers, whose share declined to 50% in 1987 from 54% in 1978.

The most significant contribution to job creation came from the smallest firms, which employed fewer than 5 people (many of them grew into larger firms, but they had fewer than five employees when they started out). These firms accounted for less than one fifth of small-business employment in 1978 but contributed half of the jobs created by small businesses between 1978 and 1988. As Table 2.1 shows, these smallest firms created almost half a million new jobs on a base of 215,000 employees in 1978. That's a growth rate of 125% over the ten years, an average of 8½% a year, or more than double the average annual growth in the Gross Domestic Product.

Table 2.1
Patterns of employment and job creation, Ontario

Distribution of employment by firm size in 1978 and 1987, and contribution by firm size toward job creation in the intervening years

Number of employees in the firms	**Employment distribution 1978**		**Share of new jobs created 1979-88**		**Employment distribution 1987***	
	(000s)	**%**	**(000s)**	**%**	**(000s)**	**%**
Fewer than 5	214.7	6.0	481.2	35.5	292.0	6.3
5 - 19	366.8	10.2	279.0	20.6	506.8	11.0
20 - 49	295.7	8.3	140.1	10.3	424.3	9.2
50 - 99	227.9	6.4	100.0	7.4	338.7	7.4
All small firms	**1,105.1**	**30.9**	**1,000.3**	**73.8**	**1,561.8**	**33.9**
100 - 499	529.8	14.8	157.4	11.6	725.7	15.8
500 or more	1,942.8	54.3	197.3	14.6	2,312.7	50.3
All firms	**3,577.7**	**100.0**	**1,355.0**	**100.0**	**4,600.2**	**100.0**

**Note: The number of employees in each size of firms in 1987 is not the sum of the number in 1978 plus the new jobs in 1979-1988. Indeed, for firms employing fewer than 5 people, the number of jobs created during 1979-88 exceeds the total jobs in these firms in 1987. This is because many of the firms grew bigger than their original size category so were reclassified in 1987. Firms are classified according to the number of people they employed when they started in business or in 1978 if they existed then.*

An accurate distribution by size of firm is not available for 1988.

The reliance on small firms was even greater in the rest of Canada, where they accounted for 88% of the new jobs over the same 10 years. This raised the share of the workforce in small firms to 39% from 35%. For the whole of Canada, as Table 2.2 shows, small firms accounted for 81% of all the new jobs created between 1978 and 1988 and employed 37% of the workforce by the end of 1987.

Table 2.2
Patterns of employment and job creation, Canada

Distribution of employment by firm size in 1978 and 1987, and contribution by firm size toward job creation in the intervening years

Number of employees in the firms	Employment distribution 1978		Share of new jobs created 1979-88		Employment distribution 1987*	
	(000s)	%	(000s)	%	(000s)	%
Fewer than 5	620.0	6.8	1,235.5	45.1	866.9	7.8
5 - 19	1,013.4	11.1	609.0	22.2	1,391.0	12.4
20 - 49	805.1	8.8	243.9	8.9	1,063.8	9.5
50 - 99	619.6	6.7	135.7	5.0	816.4	7.3
All small firms	**3,058.1**	**33.4**	**2,224.1**	**81.2**	**4,138.1**	**37.0**
100 - 499	1,428.6	15.6	269.8	9.8	1,746.4	15.6
500 or more	4,672.3	51.0	245.7	9.0	5,296.6	47.4
All firms	**9,159.0**	**100.0**	**2,739.6**	**100.0**	**11,181.0**	**100.0**

**Note: The number of employees in each size of firms in 1987 is not the sum of the number in 1978 plus the new jobs in 1979-1988. Indeed, for firms employing fewer than 5 people, the number of jobs created during 1979-88 exceeds the total jobs in these firms in 1987. This is because many of the firms grew bigger than their original size category so were reclassified in 1987. Firms are classified according to the number of people they employed when they started in business or in 1978 if they existed then.*

An accurate distribution by size of firm is not available for 1988.

In these circumstances, it would seem logical that provinces where the concentration of small firms is greatest would benefit most from the power of small firms to create employment. This is not the case with Ontario, however. Although Ontario has 50% of its workforce in big firms, compared to 45% in the rest of Canada, it still managed to achieve a much faster growth in employment over the ten years to 1988 (38% compared to 25%). It is likely that Ontario's small firms have benefitted from the strong presence of big firms, if only because the big firms have downsized their operations, abandoning market niches to smaller firms. It is even more

likely, however, that Ontario's highly developed industrial infrastructure and its geographic location, close to the major markets in the U.S., are the principal contributors to the province's strong growth. In Ontario, there's just more activity for smaller firms to capitalize on than there is in the rest of the country.

However, this still doesn't explain all of Ontario's edge over the other provinces. Governments and their agencies are important contributors to job creation. They have been hiring at an even faster rate than the private sector over the past decade.

The funded and the market sectors

In analyzing the impact of job creation by the public sector, it is helpful to expand the definition to the "funded sector", which groups public administration with community services (education, health and welfare and cultural organizations). The funded sector consists almost entirely of organizations that are not subject to direct market forces, but earn their revenues on the basis of political, charitable or other considerations. As Table 2.3 shows, almost one quarter of the Canadian workforce is in the funded sector.

In the ten years, 1979-88, employment in the funded sector grew by 36% in Canada, accounting for 27% of the new jobs during the period. By contrast, the market sector grew by 28% to account for the remaining 73% of the new jobs.

Perhaps surprisingly, the funded sector has grown significantly faster in Ontario (48%) than it has in the rest of Canada (29%) over the ten years to 1988. It would appear that the stronger the market sector is, the more comfortable governments and their agencies are likely to feel in creating - new positions. Much as governments might like to supplement the job creation of the market sector, they are constrained by more limited tax revenues when the market sector grows more slowly. The funded sector appears, in effect, to act as an employment amplifier to the market sector rather than as a primary source of new jobs. This is reinforced by the fact that, despite its slower growth rate, the funded sector accounted for a bigger share of new jobs in the rest of Canada (30%) than it did in Ontario (25%). This means, of course, that the growth gap between Ontario and the rest of the country is even greater in the market sector than the overall statistics indicate - 36% in Ontario compared to 23% in the rest of the country.

Table 2.3
The reach of the funded* sector

Distribution of jobs in 1978 and 1987 and of job creation in 1979-88 in the funded sector, and growth rates during 1979-88. Ontario, the rest of Canada and Canada

	Ontario	Rest of Canada	Canada
Number of jobs, 1978 (000s)	703.6	1,397.4	2,101.0
Share of total workforce	19.7%	25.0%	22.9%
New jobs, 1979-88 (000s)	335.6	411.5	747.1
Share of job creation	24.8%	29.7%	27.3%
New jobs, 1979-88, in organizations with 100+ employees	246.0	239.7	485.7
Share of new jobs (100+)	69.3%	147.0%	94%
Number of jobs, 1987 (000s)	987.3	1,735.1	2,722.4
Share of total workforce	21.1%	26.0%	23.9%
Growth rate 1979-88	47.7%	29.4%	35.6%
Average annual growth rate	4.0%	2.6%	3.1%

**Notes: The funded sector encompasses public administration (SIC codes 902 to 999) and community services (SIC codes 801 to 831).*

Since governments are heavily weighted toward big organizations, (86% of funded-sector jobs in Canada are in organizations with more than 100 employees), the funded sector influences statistics for job creation in big organizations to a degree far beyond its overall weight in the economy. As Table 2.3 shows, the funded sector accounted for 27% of the new jobs during 1979-88, but 94% of the new jobs in firms employing more than 100 people. In organizations employing more than 500 people, the funded sector accounted for more than 100% of the job creation in Ontario (109%) as well as the rest of Canada (319%). In other words, employment in firms in the market sector that started out in 1978 with more than 500 employees actually declined in the decade (see Table 2.4 later in this chapter).

This phenomenon of employment decline in large firms in the market sector was more pronounced in the rest of Canada (an 11% decline) than in Ontario, where it was only 3%. By contrast, small firms grew strongly to account for 98.5% of all new jobs created in Canada's market sector between 1978 and 1988. In Ontario, it was 89.3%. Small and mid-sized

firms in the market sector have clearly come to bear an enormous responsibility for the continuing growth of employment in Canada and Ontario. Not only do they create new jobs, while the big firms are downsizing, but they grow into big firms themselves, thereby diminishing the extent of the loss of jobs in big firms. Care must be taken, however, not to ascribe too much power to size alone as a determinant of capacity to create jobs. There are other important factors that make some smaller firms better job creators than others.

In the smallest firms, those employing fewer than 5 people, the remarkable increase in employment reflects a spectacular surge in new entrepreneurs. These people, for whatever reason, are rebelling against working for other people and starting their own firms in droves. Most of them are not significant creators of employment: some are "lifestyle" entrepreneurs, who want to work for themselves, not grow bigger; many others are trying to make a dream come true, but find they cannot do it or don't want to make the necessary sacrifices, so they return to being employees after a while; still others become significant job creators, but only after a long incubation while they learn the ropes. Finally, some start off with the intention of growing quickly, or they soon do so, and they grow at spectacular rates.

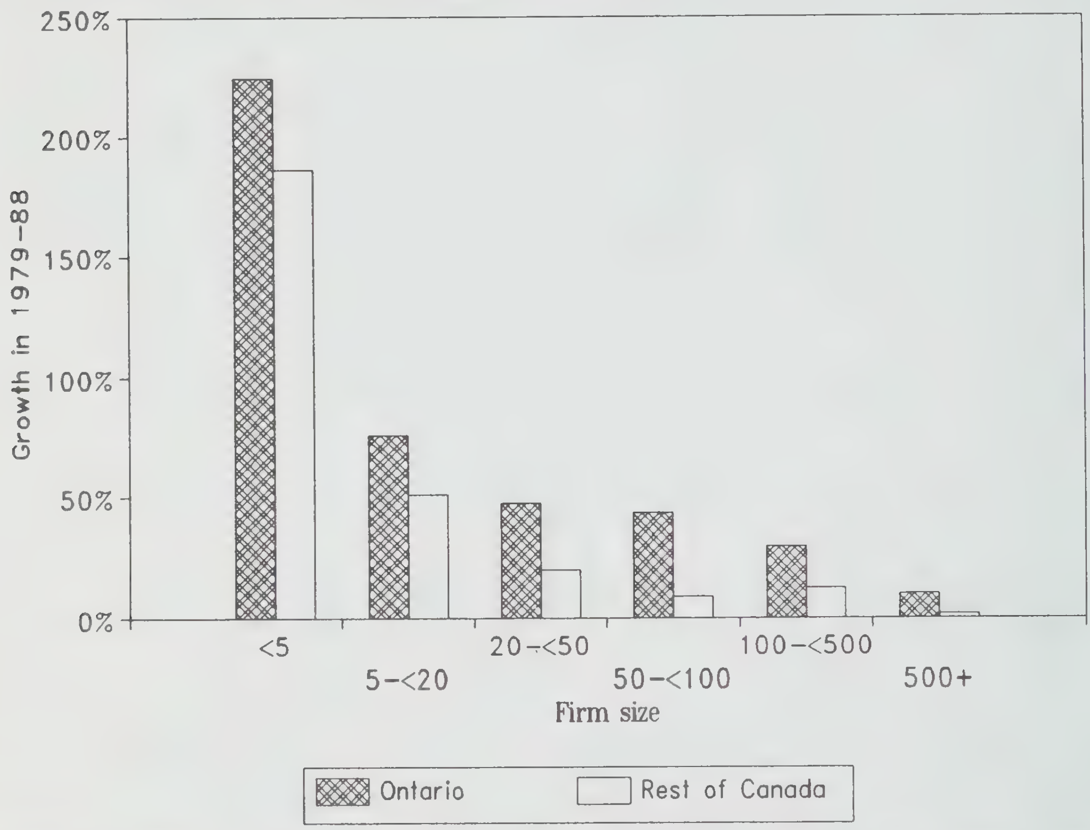
Thus, although the increases in employment are most impressive among firms with fewer than five employees, these firms are extremely vulnerable, because they are small, they lack resources and their owners are often young or inexperienced. The failure rate of these firms is very high, although many of their owners persevere to prosper in their second or third ventures. Once they survive the early stages, however, these people are the real engines of employment growth. They are a small percentage of the total, concentrated in firms that employ more than 20 people, giving them the base on which to build significant businesses.

Chart 2.2 shows that the growth rates are relatively similar for Ontario and the rest of Canada in firms with fewer than five employees, with the rest of Canada running at five-sixths the rate in Ontario. Since growth in these firms is fuelled largely by the rate of new business formation, this indicates that people are turning to self-employment at about the same rate across the country. As firms get bigger, however, the growth rate in the rest of Canada becomes smaller and smaller relative to Ontario's. For firms with five to 20 employees, it's two thirds Ontario's rate; for firms with 20 to 50 employees, 43%; for firms with 50 to 100 employees, 21%; for firms with 100 to 500 employees, 42% (the only positive aberration); and for

firms with more than 500 employees, 18%. This indicates that Ontario has more strength than the rest of Canada in these growth-oriented small firms that already employ more than 20 people, as well as in the medium-sized and large firms.

Chart 2.2
Small firms grow faster than big firms

Growth of employment in each size category for Ontario and the rest of Canada, 1979-88



This conclusion is strengthened by the statistics in Table 2.4, which show that employment in Ontario in firms with 20 to 100 employees is almost exactly the same as it is in firms with fewer than 20 employees, whereas the rest of Canada has a much higher concentration of employment in the smaller category. In proportional terms, Ontario has a smaller concentration of employment than the rest of Canada in small firms that employ fewer than 100 people, but its small firms are significantly weighted toward the bigger, more growth oriented, firms employing 20 to 100 people. In 1987, the province had only 35% of the jobs in Canadian firms

employing fewer than 20 people; but it had 42% of the jobs in Canadian firms employing 20 to 100 people.

Table 2.4
Ontario's weight in the market sector

Distribution, within the market sector, of employment in 1987 and job creation during 1979-88, by firm size, for Ontario and the rest of Canada

	Employment in 1987			Jobs created during 1979-88		
Firm size	**Ontario**	**Rest of Canada**	**Ontario as a % of Canada**	**Ontario**	**Rest of Canada**	**Ontario as a % of Canada**
(employees)	**(000s)**	**(000s)**	**%**	**(000s)**	**(000s)**	**%**
Fewer than 20	730.1	1,326.9	35.5	691.9	960.7	41.9
20 - <100	710.9	989.8	41.8	218.3	91.1	70.6
Small firms	**1,441.0**	**2,316.7**	**38.3**	**910.2**	**1,051.8**	**46.4**
100 - <500	631.9	750.9	45.7	125.8	28.8	81.4
500+	1,540.2	1,777.7	46.4	-16.9	-107.3	n/a
All firms	**3,613.1**	**4,845.3**	**42.7**	**1,019.1**	**973.3**	**51.1**

The employment growth in these larger small firms (20-100 employees) is driven less by new entrepreneurs or startups, more by internal expansion. These firms include many who started in the smallest category but grew out of it, often in spectacular fashion. Many of tomorrow's big companies are in this category today. In Ontario, these firms created 218,000 new jobs during 1978-88; in the rest of Canada, the same sized firms created only 91,000 jobs, even though the employment base from which they started in 1978 was 40% bigger than Ontario's.

It is reasonable to hypothesize that better growth rates emerge as the numbers in any category increase. In other words, as businesses of a particular size multiply, they develop synergies and common infrastructures that help them grow. It would appear that this maturing of the entrepreneurial companies employing 20 to 100 people is the source of much of Ontario's strength as a job creator relative to the rest of Canada.

Births, deaths and survivors

It has long been recognized that the formation of new businesses has been an important driving force behind Canada's impressive record of job creation in the 1980s. The new jobs created by "births" in Ontario between 1978 and 1988 represented 85% of all the new jobs created during the period - a substantial advantage over the jobs lost from corporate deaths, which subtracted the equivalent of 46% of the new jobs created.

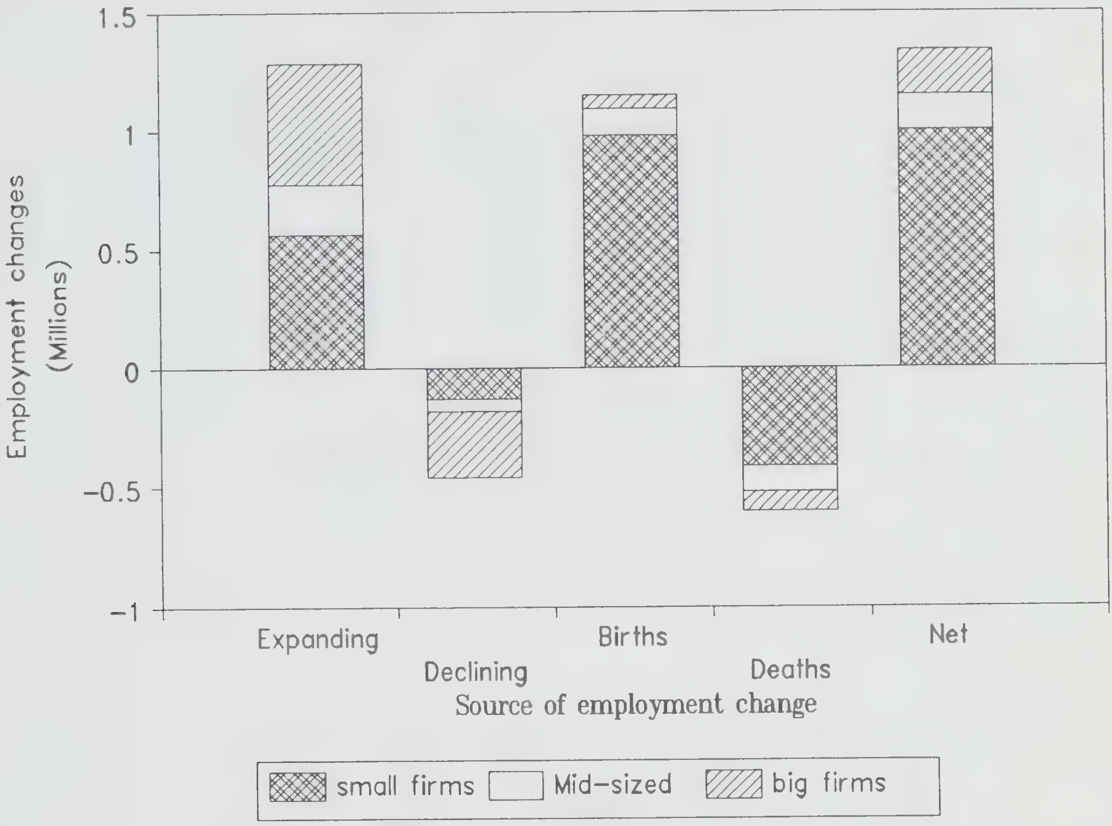
The jobs created by firms that were already in existence in 1978 is somewhat higher than this, but not much. Of the firms that existed in 1978 and were still in business in 1988, 62% had expanded their employment and 38% had contracted. The former created the equivalent of 96% of all new jobs created between 1978 and 1988, while the firms that contracted their employment lost the equivalent of 35% of the new jobs.

As Chart 2.3 shows, small firms were responsible for the bulk of job changes from births and deaths (84% and 66% respectively), while big firms dominated the job changes from the expansion or contraction of firms already in existence in 1978. Small firms accounted for 43% of the jobs created by expansions and 27% of the jobs lost from contractions.

It is perhaps more meaningful to view the jobs created and lost by births and deaths as a single unit, because the level of jobs lost from deaths is so dependent on the rate at which new firms are formed in the preceding year or two. On average, almost a quarter of new firms fail within the first year of their lives; by the end of the third year, about a half are no longer in business. In any one year, firms that die in their first year of operations account for 30% of the jobs lost by deaths. This high rate of job loss means that deaths subtracted 54% of the jobs created by births between 1978 and 1988. [Even this may be a slight understatement because the jobs lost from deaths are from firms which went into business in 1978 or earlier, and these are probably somewhat fewer than the jobs that were to disappear after 1988 from the greater number of firms that were started in 1987 or 1988.]

Chart 2.3
The contributions to job creation by births and expansions

Jobs created by firms formed during 1978-88 and by the expansion of firms existing in 1978; jobs lost from contractions or cessation of firms existing in 1978. Ontario, 1978-88

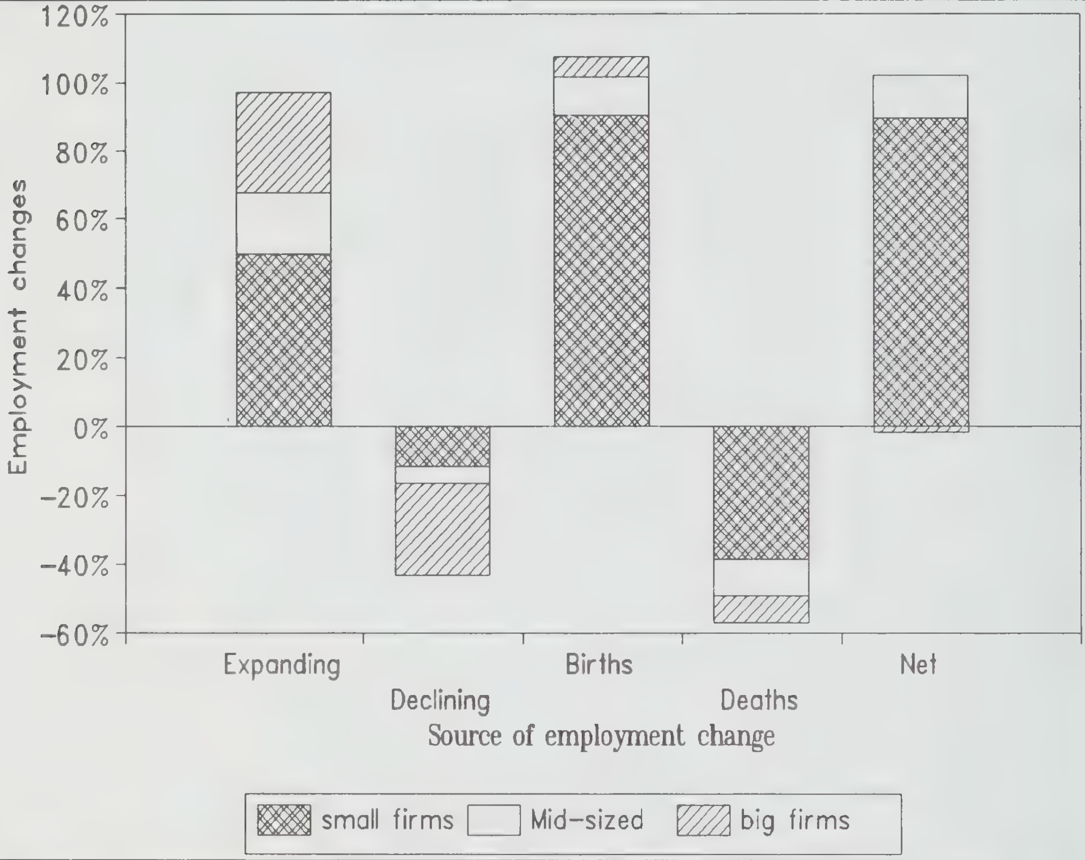


Looking at the combined effect of births and deaths, therefore, they accounted for 39% of all the jobs created between 1978 and 1988. Net job creation from expansions and contractions accounted for the other 61%. Small firms were entirely responsible for the net gain from births and deaths (in fact the jobs lost from deaths of mid-sized and large firms exceeded the jobs gained by births). Small firms accounted for 53% of the net gains from expansions and contractions.

However, these conclusions do not take account of the effect of the funded sector, which is so heavily weighted toward big organizations and which is largely insulated from the opportunities and threats that govern births and deaths in the market sector.

Chart 2.4
Job creation in the market sector by births and expansions

Share of jobs created by firms formed during 1978-88 and by the expansion of firms existing in 1978; share of jobs lost from contractions or cessation of firms existing in 1978. Ontario, 1978-88



Births are a significantly more important force in job creation in the market sector, accounting for 107% of total new jobs created during the decade to 1988. Expansions, by contrast, accounted for 97%. Births net of deaths accounted for almost half of the new jobs created (48%), and net expansions accounted for 52%. As Chart 2.4 shows, small firms assume a more dominant role in both births and expansions in the market sector, accounting for 84% of the jobs created by births and 51% of the jobs created by expansions. In net terms, small firms provided 107% of the new jobs from births net of deaths, and 73% of the new jobs from expansions net of contractions.

Clearly, the rate of new business formation is a critical factor in job creation. Over the past decade, the rising level of interest in self-employ-

ment has led to a steady rise in the number of new businesses formed every year, fuelling the remarkable record of job creation. The progression of business formations has therefore become an important indicator of job creation. There are three principal tools available for measuring startups, each with its advantages and disadvantages:

- The Employment Dynamics statistics[2] from Statistics Canada;
- New incorporations; and
- Registrations of unincorporated businesses.

Incorporations are an important concrete measure that is definitively ascertainable, but they do not identify separately the existing unincorporated businesses that are being incorporated. Registrations are a much broader measure of the degree of interest among existing and potential entrepreneurs in starting a business, but they do not measure commitment to do so.

However, Statistics Canada has developed a special statistical analysis of the Employment Dynamics statistics that corrects the major technical difficulty and also analyses failures by the year in which they started. This offers the only reasonably accurate measure of actual startups because it covers all new businesses that start hiring people. Registrations still offer the best measure of interest in entrepreneurship and appear to be an indicator of startups. Incorporations offer the best measure of businesses that are moving into a period of growth, whether they are startups or existing businesses.

Table 2.5 below shows that registrations are far more frequent than startups. Incorporations have become more frequent than startups in recent years, probably reflecting the maturity of startups five or more years previously.

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[2]These statistics include a significant number of firms that escape the statistical net for a period of one or more years. These firms are counted as failures when they are first lost and as new firms when they are included once again.

Table 2.5[3]
Measures of desire to start businesses and of decisions to do so

Number of registrations of unincorporated businesses, incorporations and startups of new firms, Ontario, 1979 to 1989.

Year	Registrations	Incorporations	Startups
1979	48,983	27,969	38,850
1980	52,745	28,394	36,459
1981	56,629	28,696	37,136
1982	60,706	28,656	32,967
1983	69,848	30,678	39,062
1984	74,314	32,110	38,364
1985	87,611	38,512	42,710
1986	106,995	45,734	45,265
1987	118,304	51,824	49,156
1988	113,486	55,657	49,635
1989	105,372	57,094	
1990*	92,880		

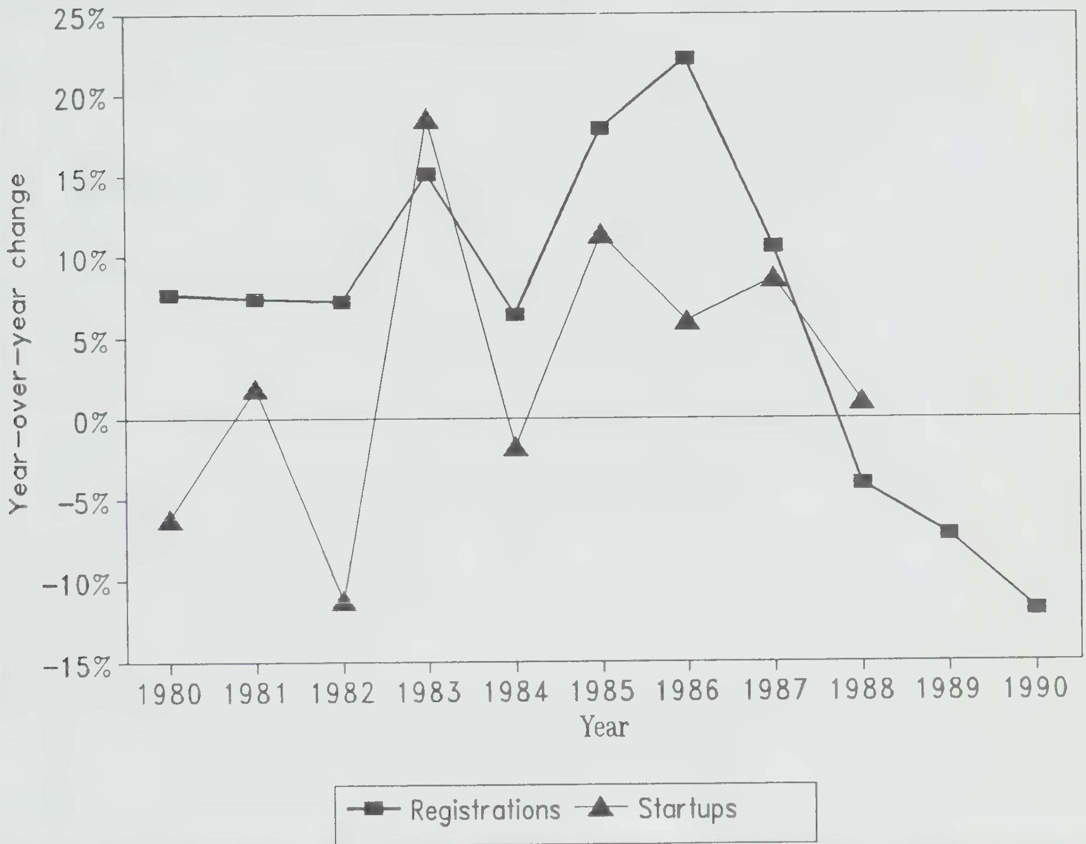
**Note: The number of registrations for 1990 is an estimate based on the results for January to August.*

It is notable that incorporations barely changed from year to year between 1979 and 1983, then started increasing rapidly until 1988 when they started levelling off. Startups followed a similar pattern delayed by one year: they were flat until 1984, before taking off in 1985, then levelling off again in 1989. A closer examination of year-over-year changes reveals some disturbing trends. Chart 2.5 shows the year-over-year increases in registrations and startups. Registrations peaked in 1987 after growing rapidly for the previous three years, then started an accelerating decline. They were not affected by the last recession, showing steady growth through 1981-83, and they were growing comfortably faster than startups. The sudden decline in registrations is now racing ahead of the decline in startups, which bodes ill for the pace of startups, since they have followed registrations reasonably faithfully in the past.

[3]Source: Ministry of Consumer and Commercial Relations, Ontario, and the Small Business & Special Surveys division of Statistics Canada, which performed a special analysis of firms exiting, by year of startup and exit, base on the Employment Dynamics, 1990

Chart 2.5[4]
Annual changes in business formation

Year-over-year changes in registrations of unincorporated businesses and in startups of new ventures, Ontario, 1979-89



This could pose serious problems for the creation of jobs in 1989 and later, since births are such an important part of job creation. It is worth noting that startups last declined as a result of the 1981-82 recession, which precipitated a sharp decline in 1982, followed by an even more sharp increase in 1983 and a small decline in 1984. This would seem to indicate the timing of startups was significantly disrupted by the recession. In 1982, when the full brunt of the recession became apparent, many entrepreneurs signalled their intention of starting a business by registering them but delayed their startups for a year to wait for economic conditions to improve. In 1983, startups surged partly because of the delayed startups

[4]Source: Ibid.

from 1982, partly because of the influx of people laid off by big firms. In 1984, startups declined again to allow the market to digest the frantic year of 1983.

In 1988, however, registrations began to decline before the current recession had even started. It seems likely, from this chart, that, when updated statistics for startups are made available next year, startups will be shown to have declined significantly in 1989, with the prospect the decline will continue at least into 1990.

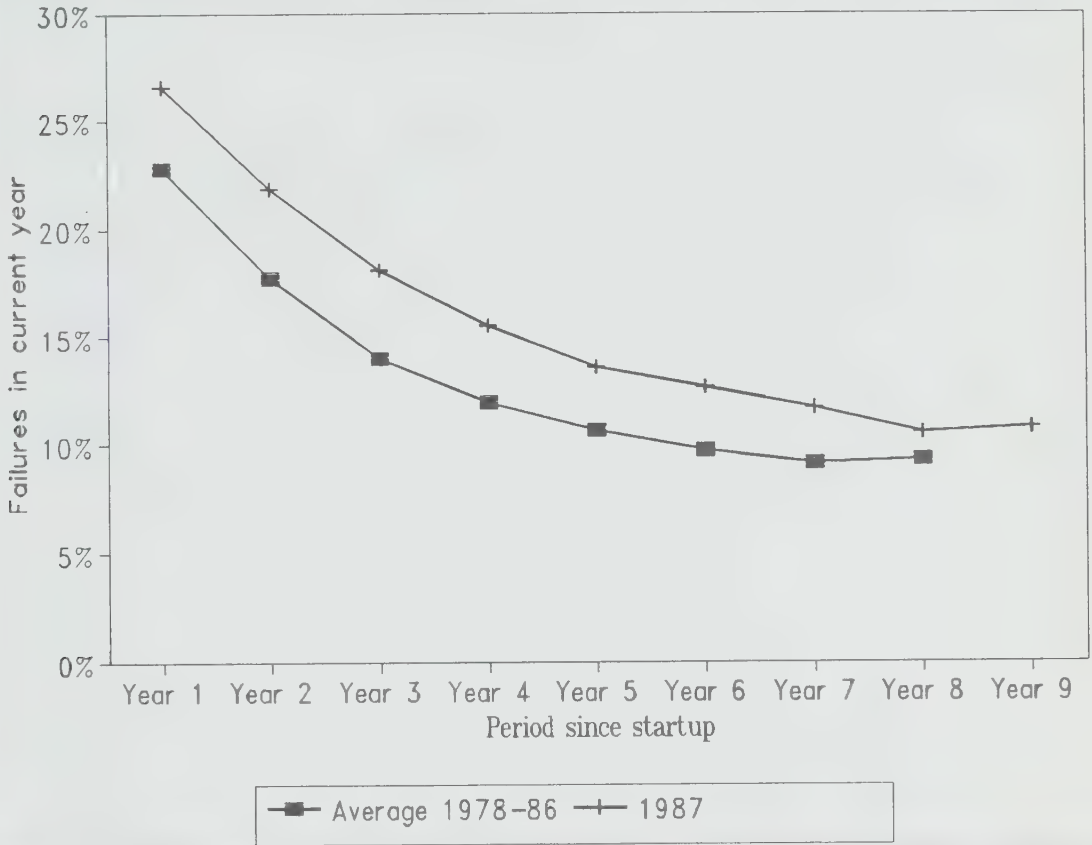
A further indicator of a deterioration in some critical trends is the rate at which firms fail. For most of the 1980s, the failure rates of new companies were reasonably consistent, although they did vary with economic conditions. As Chart 2.6 shows, the failure rate of established firms that have existed for five or more years has been about 10% of the surviving firms every year, but failure rates for younger firms have been much higher - 23% in the first year, 18% in the second, 14% in the third and 12% in the fourth. At these rates, the average life of a new firms in Ontario today is 8 years. [Before 1978, preliminary research indicates the failure rate of established firms was about 6% a year, while the rate for younger firms was somewhat higher than those for firms that started in 1978-1986.]

In 1987, however, failure rates jumped sharply to three or four percentage points higher than they had been during the previous decade. These increased failure rates applied consistently to all ages of firms, indicating a general deterioration in the resilience of small firms that goes beyond any increased volatility of younger firms. The higher failure rates in 1987 would leave only 47% of new firms still in business at the end of their third year, compared with a 55% survival rate at the failure rates that applied between 1978 and 1986.

These failure rates are far more serious than bankruptcies, which constitute only 5% to 10% of all business failures. Failures include receiverships, people who just close down their businesses because they cannot make enough profit and people who sell out to competitors (often bigger firms that reduce employment subsequently).

Chart 2.6[5]
Failure rates for young firms surge in 1987

Failure rate of businesses in existence at the beginning of each year, by years since startup, Ontario, 1987 and average for 1978-1986

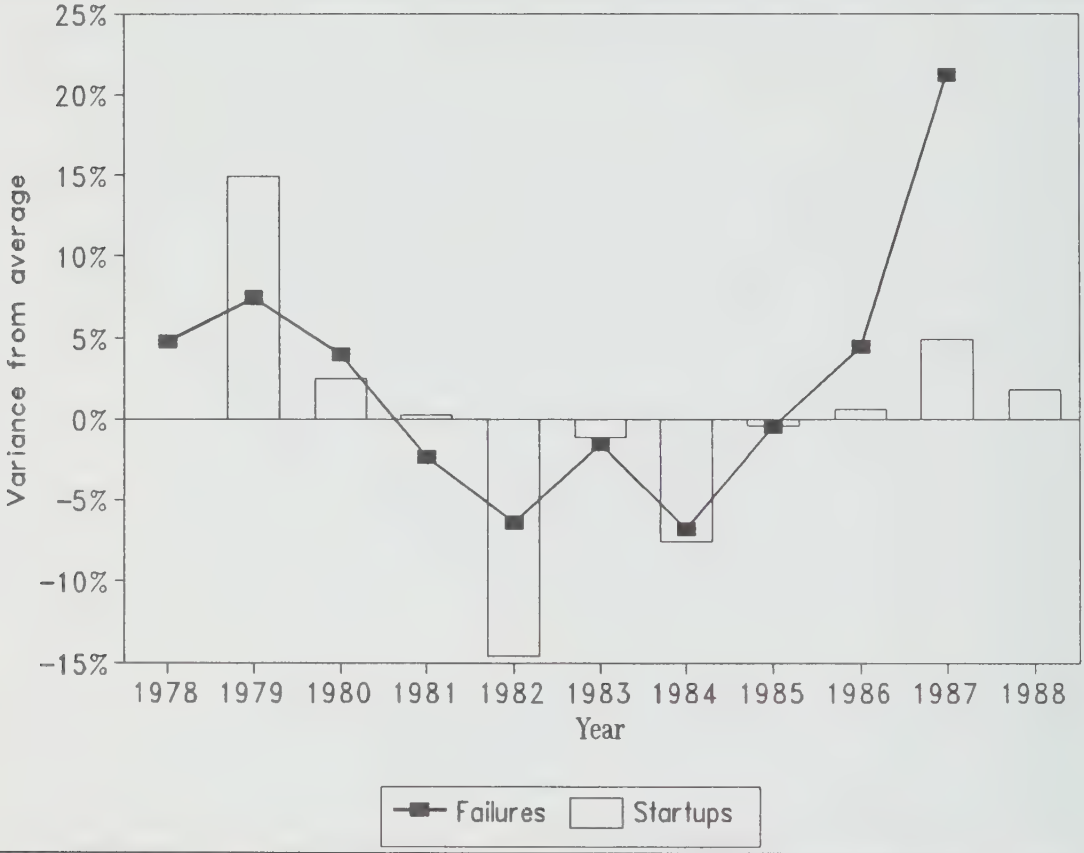


Failures are influenced most heavily by the number of startups in previous years, but they also vary with shifts in economic conditions. Chart 2.7 illustrates this phenomenon. The chart is based on the average rate of startups during the period from 1979 to 1988 and the average failure rate, by age, of firms that failed between 1978 and 1987. This enabled a calculation to be made of the startups and failures that would be expected in each year if the average rates referred to earlier were to apply to the particular mix of firms at the beginning of that year. The chart then compares the actual with the expected experience.

[5]Source: Ibid.

Chart 2.7[6]
Births and deaths in changing economic conditions

Percentage variance of the actual number from the expected number of firms starting up and dying in Ontario, 1978-89



It can be clearly seen from this chart how startups slowed in 1982 as the recession bit, before recovering to normal levels in 1985 and 1986. As might be expected, startups increased again as the 1983-89 boom stretched into 1987 - and then started to return to normal levels as the current recession approached. Presumably, startups will be shown in the next year or so to have slowed sharply in 1989 and 1990, consistent with the previous charts and tables in this chapter. The failures, however, have shown a less predictable course. From 1979 to 1985, they followed the trend of startups fairly closely, usually with a lag that kept changes in the death rates less volatile than startups. In 1986, however, the failure rates started increasing

[6]Source: Ibid.

more quickly than startups, then, in 1987, they reached a level far beyond anything that can be explained by the economic cycle. This suggests that the high failure rates in 1987 reflect a substantive change in the resilience of Ontario's firms that will reduce the net number of new firms surviving the startup stage.

Table 2.6[7]

The startup stakes - and the deaths that follow

Number of startups (1979-88) and number of firms ceasing operations (1978-87) by industry; startups expressed as an average percent of the number of firms at the beginning of each year; and exits as a percent of startups each year. Ontario

Industry	Startups 1979-88	Exits 1978-87	Startup rate %	Exits/ startups %
Mining	1,129	1,044	13.0	92.5
Primary	20,082	18,037	12.7	89.8
Retail trade	58,013	49,393	13.3	85.1
TC&U*	12,871	10,401	13.2	80.8
Construction	47,060	37,845	13.2	80.4
FIR&E*	22,113	17,619	11.5	79.7
Wholesale trade	20,279	15,827	11.4	78.0
B&P services*	118,390	90,076	17.2	76.1
Manufacturing	22,266	16,421	10.4	73.7
Community services*	19,335	11,024	8.3	57.0
Public administration	422	426	3.1	100.9
Unclassified	67,644	41,414	30.8	61.2
TOTAL	**409,604**	**309,527**	14.3	75.6

**Notes: TC&U is Transportation, Communications and Utilities; Finance, I&RE is finance, insurance and real estate; P&B services is Personal and Business services; Community services includes education, health & welfare and cultural organizations.*

It is interesting to note the degree to which there are variations in startups and deaths in different industries. On average, startups have been running at 14 new businesses for every 100 operating at the beginning of the year. And for every 100 new businesses each year there are another 76 that go out of business. Table 2.6, in which industries are ranked by the incidence of failures for each 100 startups in the market sector, shows that

[7]Source: Ibid.

the more rapid the rate of formation of new businesses the higher is the ratio of deaths to startups.

The major exception to this is business and personal services, which have the highest rate of startups but an average incidence of failures. The very large number of unclassified firms in this analysis distorts the data somewhat, but the general conclusions are probably still valid.

1988 - an aberration or the end of an era?

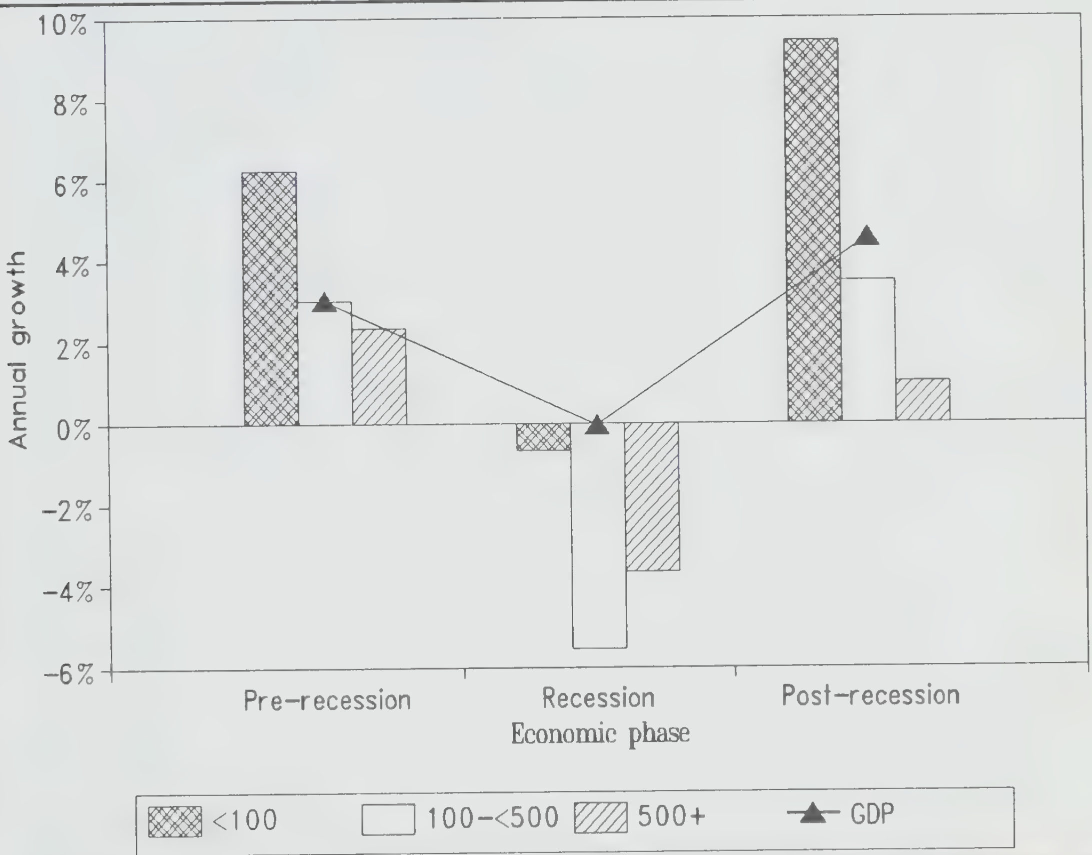
Up to the end of 1987, the trend toward a progressively greater concentration of job-creation power in small firms had appeared to be accelerating. Before the 1982-83 recession, small firms accounted for 55% of the jobs created in Canada. The two-year recession, however, changed the balance between small and large firms: big and mid-sized firms shed labour at an alarming rate of 8%, while small firms kept their layoffs to a minimum and even started adding labour in 1983, ending the two years with an employment loss of only 1.3%. In the five years since the recession, small firms accounted for 76% of the new jobs in Canada. As Chart 2.8 shows, the economy expanded more quickly after the recession than it had done before, and small firms added employment at more than twice the rate of economic expansion. By contrast, big firms expanded employment by 1% a year, compared to annual economic growth of 4.6%. The mid-sized firms expanded at about the same rate as the economy before the recession and were hardest hit by the recession; since then, they have recovered better than big firms in terms of job creation, but still lag the overall rate of economic growth by a small margin.

Within these broad trends, there are significant variations from year to year that raise the question whether the dominant role of small business in providing new jobs to the economy has peaked and will now decline. From 1984 onwards, the share of total job creation credited to small firms rose from 72% in 1984 to 91% in 1987. Then, in 1988, there was a sharp reversal as big and mid-sized employers reasserted themselves, adding almost 3½% to their workforces after growing at only slightly higher than ½% a year during the previous two years. This reduced the share of small firms in total job creation to 67% from 86% and 91% the previous two years. Since the rate of new-business formation is declining and failure rates are rising, it is possible that there has been a shift back to big organizations as the principal providers of new jobs in the economy. Conclusions cannot be drawn definitively until the statistics for an additional year or two are available, but the evidence suggests that the relative importance of small

firms has not changed - although there is still a possibility that the absolute level of job creation may be falling. What happened in 1988 is more likely a correction of distortions in previous years, within a trend that has not changed.

Chart 2.8
The evolution of job creation by firm size

Annualized growth rate of employment for small, mid-sized and big firms in the three phases of economic growth in 1979-1981, 1982-1983 and 1984-1988



The principal difficulty in interpreting job-creation statistics lies in the selection of the period over which changes are analyzed. Unlike small and mid-sized firms, big organizations in the private and public sectors tend to grow and decline in cycles that are not necessarily synchronous with the economic cycle. Because they are insulated, to a degree, from the need to respond immediately to the short-term pressures of economic downturns, big business and governments are generally influenced by factors that may have little to do with economics. Governments, for example, clamp down

on hiring when there is political pressure to do so - resulting in stable employment during recessions and slow employment growth in the early years of a boom. Government employment grows strongly only when there is a political sense that the budget deficit is not a serious problem. Since the 1981-82 recession, big businesses have demonstrated a strong inclination to slim their workforces in a wave of rationalization, takeovers and downsizing. This has had the effect of improving productivity, but is not generally sustainable. A few years of pressure on human resources soon undermines the will to make do with fewer people, culminating in bursts of hiring that compensate for the restraint of previous years. This happened two years after the 1982-83 recession and again in 1988.

As Table 2.7 shows, 1988 was a year of extraordinarily strong employment growth, particularly inn the funded sector. Small firms accounted for 75% of new jobs in the market sector, but only 67% when the funded sector is included. By contrast, in 1985, when employment in the funded sector actually declined, small firms had a bigger share of new jobs in the whole economy than they did in the market sector.

In the funded sector, hiring comfortably exceeded the total increase in employment over the previous three years combined. In the market sector, employment growth in 1988 ran at almost double the average annual rate of the previous three years.

It is likely that the strong growth in the market sector in 1988 was, to a significant degree, a reaction to the decline in employment during the previous two years of good economic growth. It is also unlikely that the strong growth in the funded sector has been maintained since 1988. It is therefore reasonable to hypothesize that the job creation statistics for 1988 should not be viewed in isolation, but as part of the five-year period since the severe cutbacks in the work force in 1982 and 1983. Furthermore, it is probable that the post-recession trends can be assessed only when the statistics for 1989 are also incorporated.

Table 2.7
Aberrations in job creation

New jobs created in Canada during 1985-88 in the funded sector and in small, medium and big firms within the market sector

	1985 (000s)	1986 (000s)	1987 (000s)	1988 (000s)
Total new jobs	388.0	351.5	407.7	717.6
- Funded sector	23.6	60.9	29.7	125.6
- Market sector	364.4	290.6	378.0	592.0
- small firms	262.4	281.1	350.3	441.3
- mid-sized firms	28.8	15.3	33.7	94.7
- big firms	73.2	-5.8	-6.0	56.0
Small-business share of jobs created				
Market sector	72%	97%	93%	75%
Total	75%	86%	91%	67%

Notes: The funded sector consists of Public Administration and Community Services (Education, Health & Welfare and Cultural Organizations)

It is particularly encouraging to note the strong performance of mid-sized firms in 1988, when they accounted for about 16% of new jobs, compared to an average of 10% in the previous three years. Although mid-sized firms follow overall economic cycles closely (as do small firms), there may be an element of catch-up in their 1988 performance, in response to a period of tight employment following the devastating effect of the 1981-82 recession. The strong 1988 means that, in the five years since that recession, mid-sized firms have increased employment only slightly slower than the growth rate of Gross Domestic Product. It will be most interesting to observe how well they weather the 1990-91 recession, because much of the growth in this part of the economy reflects the progressive maturing of the surge in new business formations of the past decade.

CHAPTER 3
INDUSTRY WINNERS AND LOSERS

Since the beginning of this century, there has been a steady and decisive switch away from goods-producing industries into service industries[1]. As recently as 1931, about 30% of the Canadian population lived on farms; by 1986, that had dropped to 4%[2], and agriculture provided employment to only 0.7% of the labour force. Less than thirty years ago, in 1961, goods-producing[3] industries employed 43.5% of the labour force. In 1987, their share had shrunk to 26% and was poised to drop still further by the end of the decade.

The slack has been taken up, of course, by services. Since the 1930s, governments and their agencies have dramatically increased their share of the country's economic output, until, by 1987, they employed almost a quarter of the labour force; wholesale and retail trade have edged ahead to employ about 19% of the labour force. Since 1961, as the goods-producing sector sharply has reduced its employment, other services in the market sector have grown strongly. Financial services have doubled their employment to 7%, a performance matched only by personal and business services, which now employ 17% of the Canadian labour force, compared to less than 10% in 1961. The stellar industry, for several years now, has been services to business management, which employed more than 6% of the Canadian labour force in 1987, compared to 1.5% in 1961.

The path of this trend is not smooth, however. The course of labour market adjustments is characterized by the radical responses of people slow to perceive changing circumstances and prone to overreact when they finally do take action. The goods-producing industries have been among the worst offenders, haemorrhaging severely in recessions, then hiring too cautiously through the recovery, before embarking on a hiring binge just before their markets were due to decline. This is happening again, as Chart 3.1 shows.

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[1]*The State of Small Business, 1989,* Annual Report on Small Business in Ontario. Chapter 8. Published by the Ministry of Industry, Trade and Technology

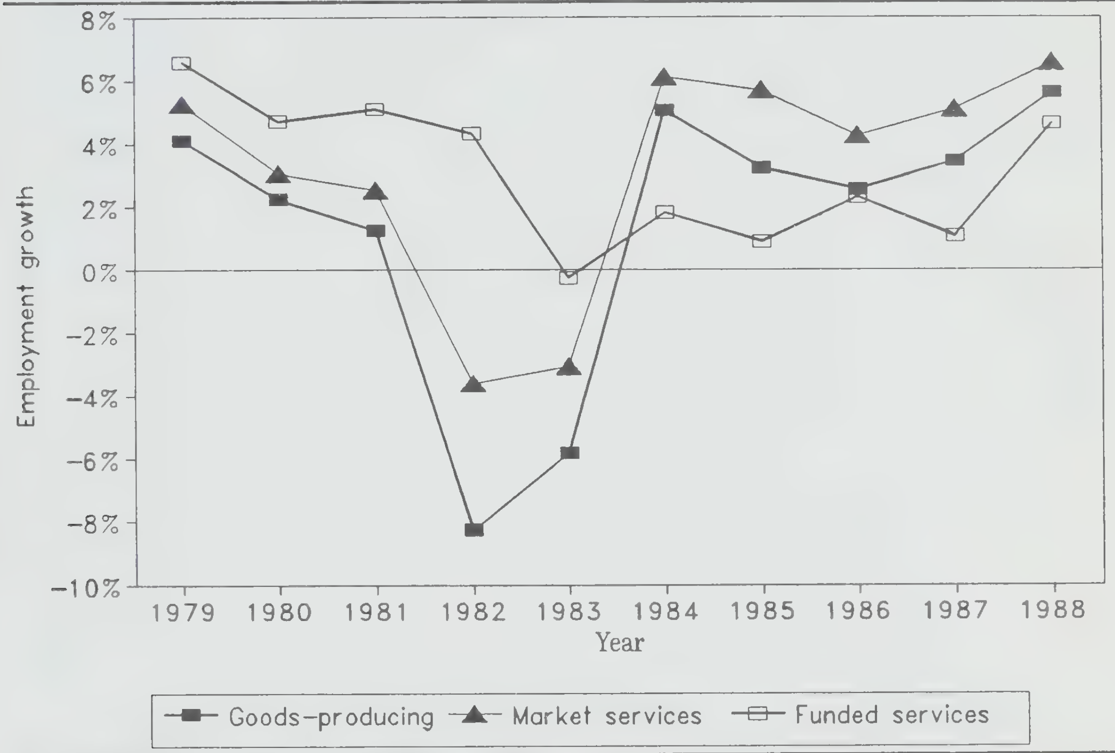
[2]Source: Canadian censuses

[3]Goods-producing industries include Primary, Mining, Manufacturing and Construction.

The goods-producing industries suffered the worst, by far, in the 1981-82 recession, cutting their workforces sharply in 1982 and 1983, then rebuilding steadily in the four subsequent years. In 1988, they threw caution to the winds and grew as fast as any other sector in a year when, as was shown last chapter, every sector was growing faster than usual.

Chart 3.1[4]
Sectoral*[5] *growth patterns in the 1980s

Annual growth rates, 1979-88, of the three main sectors



By contrast, the funded sector maintained its employment through the recession, suffering a negligible decline only when the recovery had already started, then rehiring slowly thereafter. Then this sector, too, dramatically

[4]Source: Unless otherwise stated, the data in this chapter is based on Employment Dynamics, produced by the Small Business & Special Surveys division of Statistics Canada.

[5]*Retail and wholesale trade are normally considered a separate sector, but for the purposes of charts 3.1 and 3.2, they are included with personal and business services in the market sector.*

increased its hiring. In 1988, employment growth in the funded sector was more than three times the average annual growth rate of the previous four years. Goods-producing industries had a growth rate that year two-thirds higher than the average for the previous four years. Market services, the perennial leader in the employment-growth stakes, and trade managed a growth rate of only 20% more than the average of the previous four years.

The strong growth in 1988 had the effect of raising employment in the goods-producing sector to 3,086,000, compared to 2,726,000 in 1978. However, the labour force grew much faster, so the share of the goods-producing industries in total employment fell to 26.2% in 1988, compared to 26.5% the previous year and 29.8% in 1978. Although the statistics for 1989 are not yet available, there is little doubt they will show that 1988 was the peak year in the current cycle and that employment in the goods-producing sector has declined in 1989 and 1990, just as it did in 1982-83.

The strong employment growth in 1988 did, however, have the effect of raising the goods-producing sector's share of job gains between 1978 and 1988 to 13.6%. In the nine years to 1987, its share had been 9.4%[6]. As was shown in Chapter 2, however, the surge of hiring in 1988 is most appropriately viewed as a phenomenon related to the tight hiring practices of the previous four years, so the year should be viewed in the context of one complete economic cycle in order to obtain the most accurate perception of the sources of job creation among the main sectors. Since 1981 was, like 1989, the last year of growth before a recession, it is reasonable to consider 1981-88 as a complete economic cycle. As Chart 3.2, shows, the goods-producing sector accounted for 10.2% of the new jobs during this cycle.

The slack was taken up by the other three sectors in fairly even proportions, with trade showing the greatest gains relative to its initial employment base in 1978 and market services the least.

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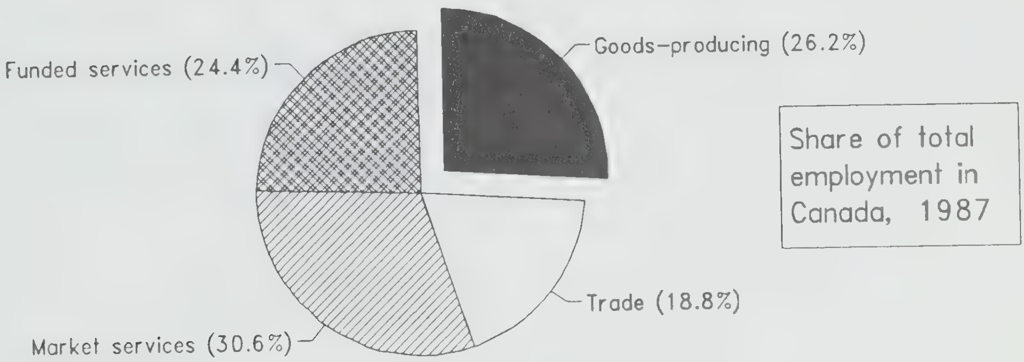
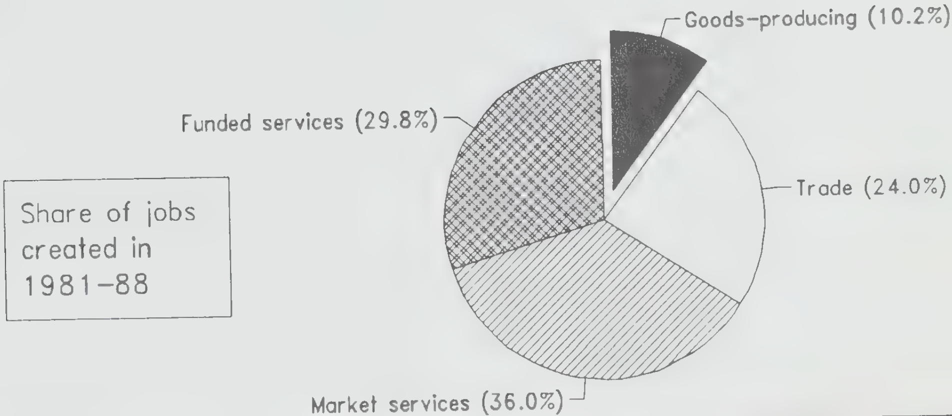
[6]Ibid. *The State of Small Business, 1989.*

Chart 3.2
The shrinking goods-producing sector

Distribution of total jobs in 1987 and share of jobs created during 1981-88 for the four sectors of the economy, Canada



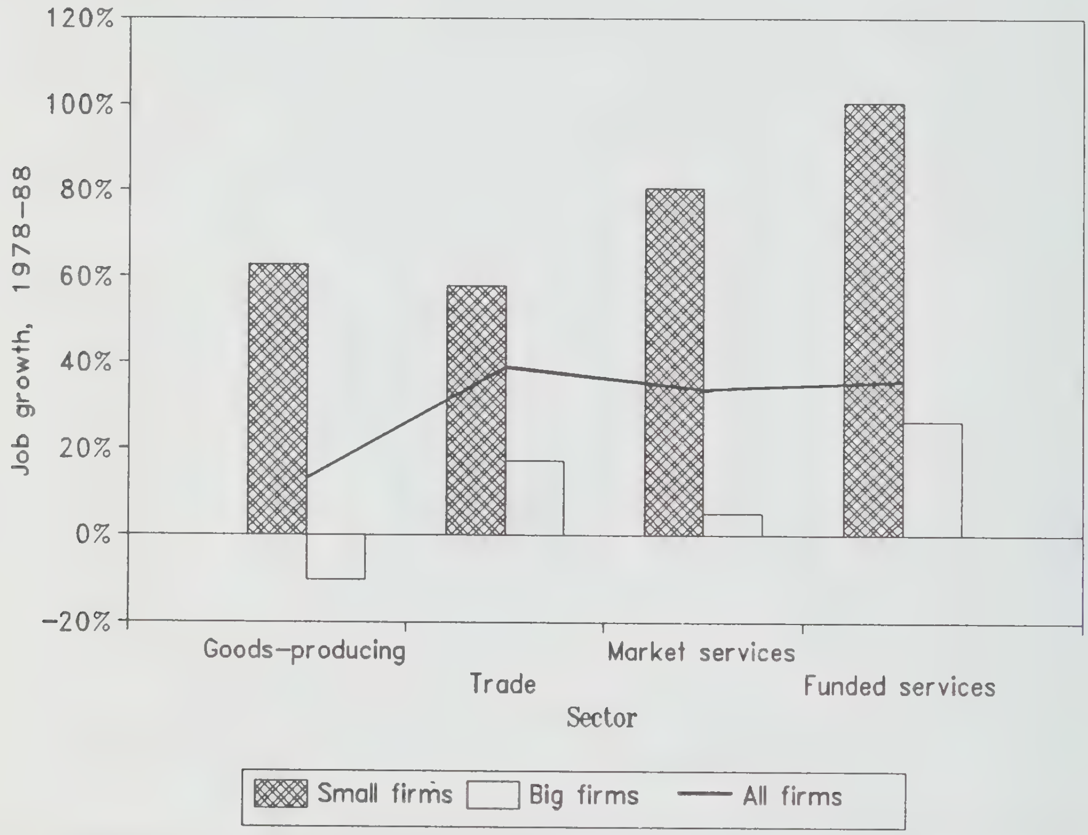


The performance of market services is a bit surprising, since this has been considered a major source of employment growth. Chart 3.3 offers the explanation. Small firms in market services enjoyed the most impressive growth of all the sectors - 80% over the decade. (The small firms in the funded sector employed only 37,000 people in 1987, so they are statistically insignificant.) But big firms in market services barely grew at all, eking out only 5%, compared to their counterparts' 26% in funded services and 17% in trade. The only industry where big firms in market services showed much growth was services to business, the star performer in the employment stakes in recent years. The big firms in this industry employed only 18% of the people employed by big firms in market services in 1987, but

they accounted for 99.4% of the new jobs created by big firms in market services during 1978-88. Other service industries had respectable gains, particularly financial companies, but their gains were wiped out by major cutbacks in the big firms in communications and transportation.

Chart 3.3
Small firms grow jobs faster than big firms in every sector

Employment growth for small firms employing fewer than 100 people and for big firms, by sector, 1978-88, Canada



As has been discussed already, employment declined over the decade in big firms in the goods-producing industries, shifting the percentage of employment in big firms to 62% in 1987 from 68% in 1978.

It may therefore be concluded that small firms are creating jobs at an impressive rate in all sectors of the economy, but big organizations are growing only in the funded sector and, to a limited degree, in retail trade. This is resulting in a shrinking employment base in industries dominated by big firms.

Industries dominated by big and small firms

The remarkable disparity between the growth rates of big and small firms raises the intriguing question of synergy between the two in generating new jobs. For the purposes of this analysis, the 51 sub-industries[7] within the four sectors were separated into those in which the small firms employed more or less than 50% of the total workforce. If more than 50% of the total employment in an industry is in small firms, that sub-industry is defined as small-firm dominated. Chart 3.4 shows that almost half of all employment in Canada is in small-firm dominant industries.

Of the 51 sub-industries, 19 (or 37%) were found to have more than half their employment in 1987 in small firms[8]. Between them, they employed 5.3 million people, or 47% of the total labour force. Obviously, the funded sector is dominated almost entirely by large organizations and the goods-producing sector is heavily weighted toward big firms. Trade and market services are the sectors where small firms are most dominant.

When the growth rates for all firms, big and small, are examined, it becomes apparent that both big and small firms grow more quickly in small-firm dominated industries than in big-firm dominated industries. Chart 3.5 shows that the three market-based sectors all enjoyed significantly greater growth in small-firm dominated industries (trade has no big-firm dominated industries). Taking all four major sectors together, the small-firm dominated half of the economy grew 45% over the decade, compared to 18% in the big-firm dominated part.

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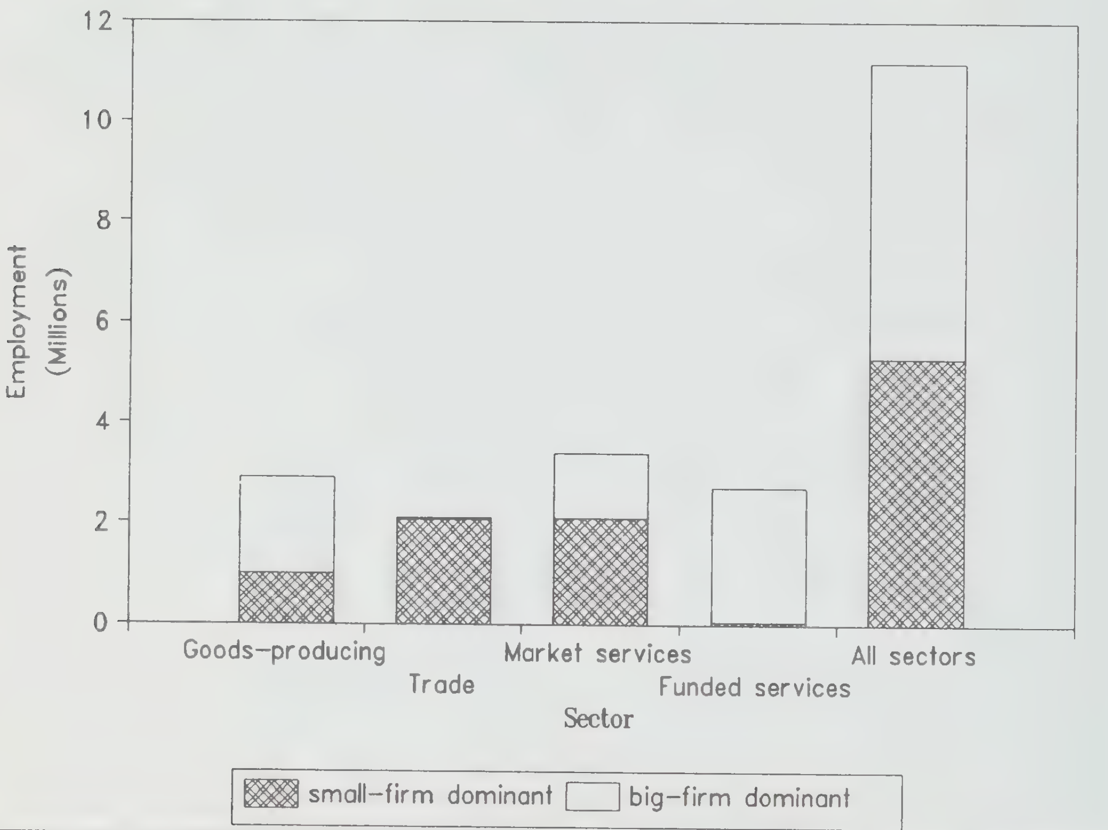
[7]Two-digit SIC codes

[8]In two industries, services to business and clothing manufacturing, the percentages in Statistics Canada's Employment Dynamics were slightly below 50%. However, these statistics exclude the owner-operators of unincorporated firms and their inclusion would take the percentage in both industries over the 50% mark.

Chart 3.4
Half the labour force is in industries where small firms dominate

Distribution of total employment between industries dominated* by small or big firms, 1987, Canada

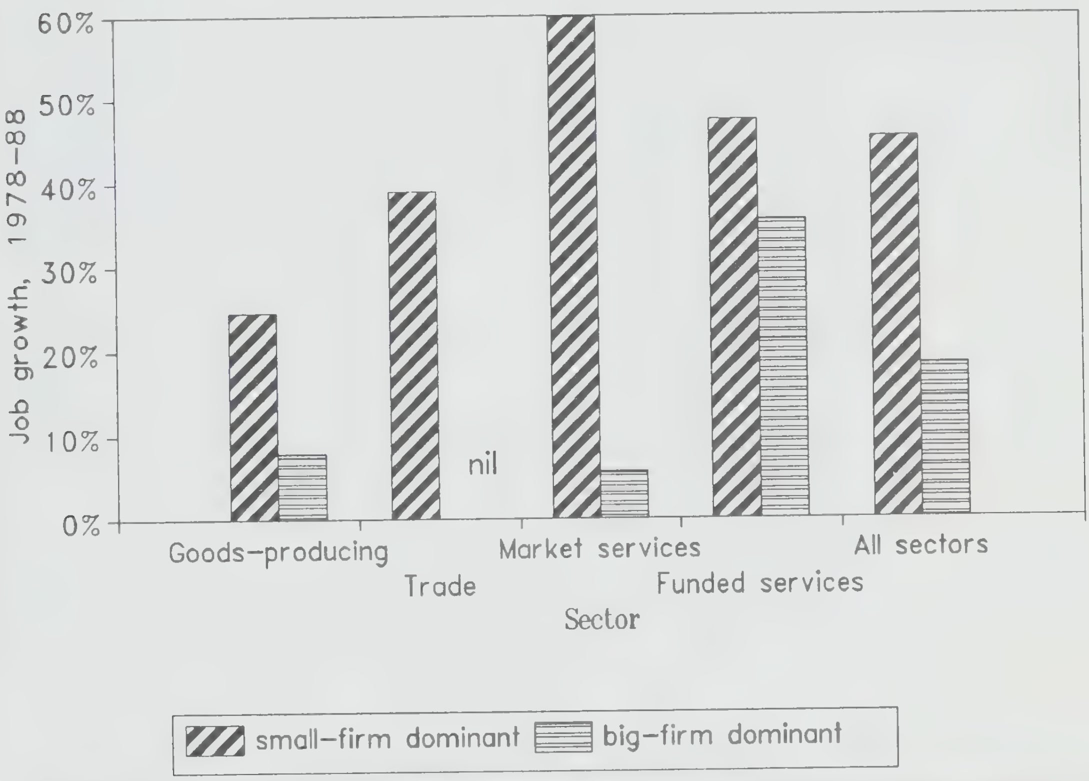


**Note: An industry is considered to be dominated by small firms when 50% or more of the total employment in the industry is in firms employing fewer than 100 people.*

The most intriguing observation, as shown in Chart 3.6, is that big firms grow more quickly in industries where small firms dominate (12.5% compared to 7% in big-firm dominated industries), while small firms grow more quickly in big-firm dominated industries (83% compared to 69% in small-firm dominated industries).

Chart 3.5
Industries where small firms dominate create jobs faster

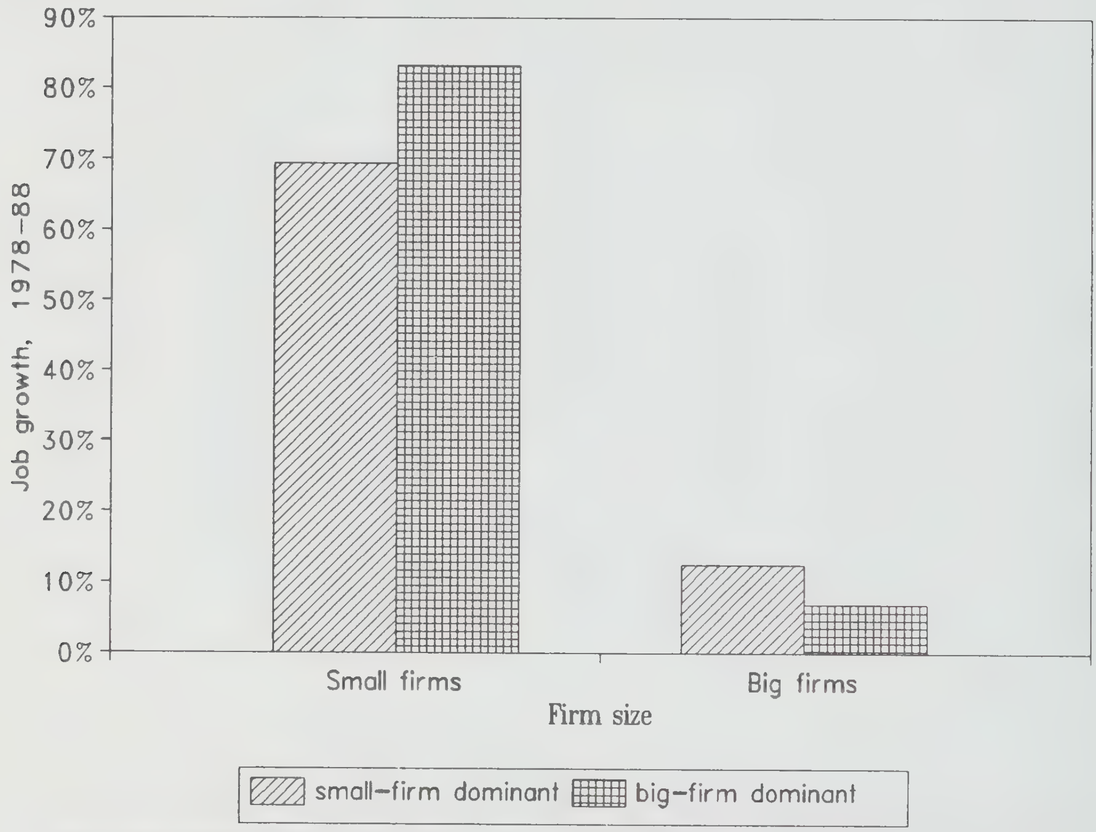
Employment growth for all firms in those industries within a sector that are dominated either by small firms and or by big firms, 1978-88, Canada



The phenomenon of big-firm growth is a mix of contrary results in the goods-producing sector (where big firms prospered in big-firm dominated industries)) and the market services sector (where big firms suffered in the big-firm dominated industries). In market services, the big firms in the big-firm dominated part of the sector declined 6% over the decade, while their counterparts in the small-firm dominated part of the sector grew 26%. In the goods-producing sector, however, the big firms in the big-firm dominated industries suffered less grievous losses in employment than their counterparts in the small-firm dominated part of the sector - they declined only 7% in the decade to 1988, compared to a 24% decline by big firms in the small-firm dominated industries.

Chart 3.6
Even big firms grow faster when small firms are dominant

Employment growth, by firm size, in industries dominated by small firms or big firms, all sectors, 1978-88, Canada



In the small-firm dominated sub-industries of the goods-producing sector, the big firms made devastating cutbacks in the workforces. Big general contractors declined 41%, clothing manufacturers 31%, metal fabricators 26% and logging companies 23%. The employment declines in large firms in metal fabricating and clothing manufacturing were so great compared to those of the small firms in these industries that the percentage of employees in big firms declined from more than 50% at the beginning of the decade to less than 50% at the end, making the industries small-firm dominated for the first time. The percentage of employees in small firms was 40% and 44% respectively in 1978 and more than 50% in 1987. In the big-firm dominated part of the goods-producing sector, large firms shed labour rapidly in many cases, too, but they were balanced by positive results in printing and publishing (18% employment growth), mineral fuels

(12%) and transportation equipment (which had only 2.5% growth, but as it is a major employer, this had a powerful effect on employment levels generally).

Turning to the small firms, the more rapid growth in big-firm dominated industries may be because they are capitalizing on opportunities for business flowing from the downsizing of big firms. Or it may be because the big-firm dominated industries tend to be less flexible in responding to market changes, so small firms can create more opportunities. Either way, it's the small firms that are taking the lead in creating employment. They are mitigating the employment effects of industries dominated by declining big firms and they are leading the job creation process in industries where they already dominate.

Ontario's role in Canadian job creation

The widely differing patterns observed above in the four main sectors of the labour force are multiplied when smaller industrial groupings are considered and when Ontario is compared to the rest of Canada. Looking first at the number of firms in Ontario and in the rest of Canada, Tables 3.1 and 3.2 show the distribution by size of firm and by industry.

There were more than 885,000 firms in Canada in 1987, about 304,000 of them in Ontario, and 581,000 in the rest of Canada. The major differences between the two include:

- Ontario has, proportionally, five times as many big organizations as the rest of Canada - 0.5% of firms compared to 0.1%.

- The rest of Canada is much heavier in small firms, which account for 99.2% of its total, compared to 97.8% in Ontario. The rest of Canada also has more firms proportionally than Ontario, which has 34% of all the firms in Canada and 41% of employment.

- Primary industries are more important to the rest of Canada - they account for 10.6% of the total number of firms, compared to 5.8% in Ontario. This is mainly because of farming, but logging and fishing operations are also much more important elsewhere in Canada than they are in Ontario.

- Ontario has a much stronger presence in manufacturing, which accounts for 7.7% of its firms, compared to 5.6% in the rest of Canada.

Table 3.1
Number of firms in Ontario, by firm size and industry

The number of firms in each industry, 1987; each industry's share of the total number of firms in all industries; and the concentration within each industry of small, medium and large firms. Ontario.

Industry	**Share of total firms**	**Number of firms**	**Percent of firms that are: Small**	**Medium**	**Big**
	%	(000s)	%	%	%
Primary	5.8	17,610	99.9	0.1	0.0
Mining	0.3	913	87.5	7.0	5.5
Manufacturing	7.7	23,516	91.4	6.4	2.2
Construction	12.7	38,806	99.2	0.8	0.0
Goods-producing	**26.5**	**80,845**	**96.9**	**2.4**	**0.7**
Wholesale trade	6.6	19,938	97.0	2.6	0.4
Retail trade	15.7	47,884	98.8	1.0	0.2
Trade	**22.3**	**67,822**	**98.2**	**1.5**	**0.3**
TC&U*	3.6	10,872	96.8	2.4	0.8
Finance, I&RE*	7.0	21,327	97.9	1.5	0.6
P&B services*	27.7	84,383	98.6	1.1	0.3
Market services	**38.3**	**116,582**	**98.3**	**1.3**	**0.4**
Community services*	8.9	26,996	97.3	1.6	1.1
Public Administration	0.4	1,131	87.0	7.2	5.8
Funded services	**9.3**	**28,127**	**96.9**	**1.9**	**1.2**
Unclassified	3.6	11,021	99.9	0.1	0.0
ALL INDUSTRIES	**100.0**	**304,397**	**97.8**	**1.7**	**0.5**

**Notes: TC&U is Transportation, Communications and Utilities; Finance, I&RE is finance, insurance and real estate; P&B services is Personal and Business services; Community services includes education, health & welfare and cultural organizations.*

Table 3.2
Number of firms in the rest of Canada, by firm size and industry

The number of firms in each industry, 1987; each industry's share of the total number of firms in all industries; and the concentration within each industry of small, medium and large firms. The rest of Canada.

Industry	Share of total firms	Number of firms	Percent of firms that are: Small	Medium	Big
	%	(000s)	%	%	%
Primary	10.6	61,839	100.0	0.0	0.0
Mining	0.8	4,684	97.4	2.3	0.3
Manufacturing	5.6	32,616	97.1	2.7	0.2
Construction	11.1	64,286	99.7	0.3	0.0
Goods-producing	**28.1**	**163,425**	**99.2**	**0.7**	**0.1**
Wholesale trade	5.6	32,642	99.3	0.6	0.1
Retail trade	17.1	99,412	99.6	0.4	0.0
Trade	**22.7**	**132,054**	**99.5**	**0.5**	**0.0**
TC&U*	4.7	27,336	99.2	0.7	0.1
Finance, I&RE*	5.7	33,212	99.4	0.5	0.1
P&B services*	26.5	153,833	99.5	0.5	0.0
Market services	**36.9**	**214,381**	**99.4**	**0.5**	**0.1**
Community services*	8.2	47,670	97.1	2.2	0.7
Public Administration	0.8	4,357	95.1	3.7	1.2
Funded services	**9.0**	**52,027**	**96.9**	**2.3**	**0.8**
Unclassified	3.3	19,351	99.9	0.1	0.0
ALL INDUSTRIES	**100.0**	**581,238**	**99.2**	**0.7**	**0.1**

**Notes: TC&U is Transportation, Communications and Utilities; Finance, I&RE is Finance, insurance and real estate; P&B services is Personal and Business services; Community services includes education, health & welfare and cultural organizations.*

The numbers of firms reflect the level of entrepreneurial activity, or the number of people who have started businesses. Ontario's relatively small share of firms seems to indicate a lower level of activity, but they employ an average of 5.3 people per firm, compared to 5.1 in the rest of Canada. Tables 3.3 and 3.4 show the number of employees and their distribution by firm size as well as between industries, for Ontario and the rest of Canada.

Table 3.3
Jobs in Ontario, by firm size and industry

The number of employees in each industry, 1987; each industry's share of total employment in all industries; and the concentration of employment within each industry in small, medium and large firms. Ontario.

Industry	Share of total jobs	Number of jobs	Share of jobs by firm size Small	Medium	Big
	%	(000s)	%	%	%
Primary	0.7	32.4	86.8	11.7	1.5
Mining	1.0	46.7	13.3	12.4	74.3
Manufacturing	22.5	1,036.6	24.5	21.9	53.6
Construction	4.9	225.6	71.4	19.4	9.2
Goods-producing	**29.1**	**1,341.3**	**33.5**	**20.9**	**45.6**
Wholesale trade	5.6	257.6	54.6	24.1	21.3
Retail trade	13.0	595.8	45.2	11.8	43.0
Trade	**18.6**	**853.4**	**48.0**	**15.5**	**36.5**
TC&U*	6.5	297.2	20.0	13.5	66.5
Finance, I&RE*	7.1	328.1	27.3	13.4	59.3
P&B services*	16.9	777.1	53.7	17.3	29.0
Market services	**30.5**	**1,402.4**	**40.4**	**15.6**	**44.0**
Community services*	13.4	618.0	17.4	12.8	69.8
Public Administration	8.0	369.3	3.5	4.0	92.5
Funded services	**21.5**	**987.3**	**12.2**	**9.5**	**78.3**
Unclassified	0.3	16.0	96.2	3.8	0.0
ALL INDUSTRIES	**100.0**	**4,600.4**	**33.9**	**15.8**	**50.3**

**Notes: TC&U is Transportation, Communications and Utilities; Finance, I&RE is finance, insurance and real estate; P&B services is Personal and Business services; Community services includes education, health & welfare and cultural organizations.*

As might be expected, Ontario has relatively more jobs in goods-producing industries mainly because of manufacturing, which accounts for 22.5% of total employment in the province, compared with 15.9% in the rest of the country.

Table 3.4
Jobs in the rest of Canada, by firm size and industry

The number of employees in each industry, 1987; each industry's share of total employment in all industries; and the concentration of employment within each industry in small, medium and large firms. Rest of Canada.

Industry	Share of total jobs	Number of jobs	Share of jobs by firm size Small	Medium	Big
	%	(000s)	%	%	%
Primary	1.4	90.1	93.3	5.9	0.8
Mining	2.2	142.7	21.9	21.6	56.5
Manufacturing	15.9	1,048.2	30.2	22.8	47.0
Construction	4.5	300.2	78.6	13.9	7.5
Goods-producing	**24.0**	**1,581.2**	**42.3**	**20.0**	**37.7**
Wholesale trade	5.5	359.2	60.0	20.4	19.6
Retail trade	13.3	878.5	55.6	9.9	34.5
Trade	**18.8**	**1,237.7**	**56.9**	**13.0**	**30.1**
TC&U*	7.5	490.1	22.9	10.2	66.9
Finance, I&RE*	6.7	443.4	29.5	10.7	59.8
P&B services*	16.2	1,069.1	63.5	16.4	20.1
Market services	**30.4**	**2,002.6**	**46.1**	**13.6**	**40.3**
Community services*	16.3	1,071.3	21.0	21.9	57.1
Public Administration	10.1	663.8	5.2	5.5	89.3
Funded services	**26.4**	**1,735.1**	**15.0**	**15.6**	**69.4**
Unclassified	0.4	23.8	95.0	5.0	0.0
ALL INDUSTRIES	**100.0**	**6,580.4**	**39.2**	**15.5**	45.3

**Notes: TC&U is Transportation, Communications and Utilities; Finance, I&RE is finance, insurance and real estate; P&B services is Personal and Business services; Community services includes education, health & welfare and cultural organizations.*

Other observations in the comparison between Ontario and the rest of Canada include:

- Despite having the federal government within its borders, Ontario's labour force has a significantly lower percentage of employees in the funded sector. This is partly a reflection of the province's greater

strength in the market sector rather than the rest of Canada's greater dependence on the funded sector for jobs. Nonetheless, 36% of the employees in Canada's funded sector are in Ontario, which has 41% of the total labour force.

- Employment in big firms with more than 500 employees is significantly higher in Ontario's goods-producing and trade sectors than it is in the rest of the country. In mining, 74% of Ontario's workforce is in big companies, compared to 56% in the rest of Canada. In manufacturing, big companies employ 54% of the province's workforce, compared to 47% elsewhere.

- Small firms account for only one third of the employment in Ontario's goods-producing sector, compared to 42% in the rest of Canada. In manufacturing, small firms employ less than one quarter of the work force in Ontario, compared to 30% in the rest of the country.

- In the market sector as a whole, small firms employ almost half the total labour force in the rest of Canada, compared to Ontario's 40%. With 43% employed in big firms in the market sector in 1987, Ontario still has more people in firms employing more than 500 than in firms employing fewer than 100, but this is likely to be reversed by the time 1990 statistics are available. The rest of Canada passed this point some time ago and had 48% in small firms and 37% in big firms in 1987.

Turning to the job-creation performance of the Canadian economy, Ontario accounted for half of all the new jobs created in Canada between 1978 and 1988, although its share of the labour force in 1987 was only 41%. Table 3.5 shows that Ontario's better performance rests principally on the goods-producing sector, particularly manufacturing. Almost 18% of the new jobs created between 1978 and 1988 in Ontario were in the goods-producing sector, compared to 8.5% in the rest of the country. In absolute terms, Ontario created more than twice as many jobs in the goods-producing sector as the rest of Canada, thanks largely to manufacturing (eight times as much as the rest of Canada) and construction (two and a half times as much).

Table 3.5
The industries that deliver new jobs: Ontario & the rest of Canada

Increase in employment, by industry, and distribution between industries, 1978-88, Ontario and the rest of Canada

	Job gains, 1978-88, in:			
	Ontario		Rest of Canada	
Industry	**Number** (000s)	**Share** %	**Number** (000s)	**Share** %
Primary	9.5	0.7	36.3	2.6
Mining	-1.4	-0.1	25.5	1.8
Manufacturing	132.5	9.8	16.1	1.2
Construction	102.3	7.5	39.5	2.9
Goods-producing	**242.9**	**17.9**	**117.4**	**8.5**
Wholesale trade	88.1	6.5	67.1	4.9
Retail trade	205.6	15.2	265.1	19.1
Trade	**293.7**	**21.7**	**332.2**	**24.0**
TC&U*	-32.2	-2.4	-9.8	-0.7
Finance, I&RE*	119.0	8.8	83.6	6.0
P&B services*	353.6	26.1	403.6	29.2
Market services	**440.4**	**32.5**	**477.4**	**34.5**
Community services	203.9	15.1	302.9	21.9
Public Administration	131.7	9.7	108.6	7.8
Funded services	**335.6**	**24.8**	**411.5**	**29.7**
Unclassified	42.1	3.1	46.3	3.3
ALL INDUSTRIES	**1,354.7**	**100.0**	**1,384.8**	**100.0**

**Notes: TC&U is Transportation, Communications and Utilities; Finance, I&RE is finance, insurance and real estate; P&B services is Personal and Business services; Community services includes education, health & welfare and cultural organizations.*

This does not mean the other sectors were weak in Ontario, however, just that Ontario's higher growth rate was more pronounced in the goods-producing sector than elsewhere. Trade, market services and funded services all delivered comparable employment gains for the province; with a labour force equal to 69% of the labour force in the rest of Canada,

Ontario delivered an average of about 88% of the gains that these three sectors made in the rest of Canada.

These results are a bit misleading because the surge of employment in 1988 distorts the picture. Since manufacturing declined sharply after 1988, this imbalance will be seen to have righted itself once the statistics for 1989 and 1990 are known.

The funded sector also followed different paths in Ontario and the rest of the country. Despite a smaller percentage of its labour force in public administration (8% compared to 10%), Ontario added 20% more jobs in governments and their agencies during 1978-88 than did the rest of Canada. As was mentioned in the previous chapter, a successful market sector supports employment growth in the funded sector. By contrast, in community services, Ontario's employment gains were significantly less than those of the rest of the country. Overall, however, Ontario still grew more quickly than the other provinces in the funded sector.

When these divergences are expressed as employment growth rates, Table 3.6 shows that Ontario's growth in the goods-producing and funded sectors is significantly higher than elsewhere - 21% and 48% respectively, compared to 8% and 29% in the rest of Canada. In Public administration, the province's employment grew 54% over the decade, compared to 19% in the rest of Canada; in construction, it grew 65%, compared to 14% in the rest of the country. The other notable performances were in finance, insurance and real estate, with growth of 51.5% and personal and business services (72%).

In small firms, Ontario's growth rate for all industries was 90.5%, compared to 63% in the rest of Canada. The most impressive growth rates came from finance, insurance and real estate (117% over the decade, compared to 61% in the rest of the country) and personal and business services (98% compared to 76.5%). (The growth in mining and community services was higher, but these industries have a very small base of small firms, so the growth rates are not statistically significant.) Once again, when the statistics for 1989 and 1990 are available, finance, insurance and real estate will not look as good, because the finance industries (the investment houses initially, and the real estate brokers latterly) were so hard hit in these two years.

Table 3.6
Small firms outgrow big firms by a wide margin

Employment growth rates for small firms employing fewer than 100 people and big firms employing 100 or more, for Ontario and the rest of Canada, 1978-88

	Employment growth rate, 1978-88, for firms employing:					
	fewer than 100		100 or more		All firms	
Industry	Ontario	Rest of Canada	Ontario	Rest of Canada	Ontario	Rest of Canada
	%	%	%	%	%	%
Primary	39.0	69.8	42.1	-17.4	39.3	59.9
Mining	137.5	150.0	-17.7	-6.4	-2.8	20.5
Manufacturing	84.2	45.8	-4.1	-13.9	14.1	1.5
Construction	92.5	38.8	4.8	-40.9	64.7	13.7
Goods-producing	**84.6**	**49.7**	**-4.2**	**-15.6**	**20.7**	**7.6**
Wholesale trade	71.0	35.9	8.8	-2.5	42.9	20.7
Retail trade	70.9	58.1	28.8	19.9	48.4	40.8
Trade	**70.9**	**50.2**	**23.0**	**13.1**	**46.6**	**34.1**
TC&U*	86.0	46.7	-24.2	-12.9	-9.3	-1.9
Finance, I&RE*	116.8	60.7	27.5	7.1	51.5	21.8
P&B services*	97.6	76.5	41.7	19.1	72.4	54.7
Market services	**99.3**	**69.6**	**9.6**	**1.8**	**41.3**	**29.1**
Community services	117.2	106.5	31.0	21.6	44.5	36.8
Public Administration	44.4	50.0	54.2	17.3	53.7	18.9
Funded services	**106.3**	**97.3**	**39.7**	**19.6**	**47.7**	**29.4**
Unclassified	n/a	n/a	n/a	n/a	n/a	n/a
ALL INDUSTRIES	**90.5**	**62.7**	**14.4**	**4.4**	**37.9**	**24.8**

**Notes: TC&U is Transportation, Communications and Utilities; Finance, I&RE is finance, insurance and real estate; P&B services is Personal and Business services; Community services includes education, health & welfare and cultural organizations.*

In firms employing 100 or more people, Ontario, as might have been expected from previous analysis, performed significantly better in the goods-producing sector. In manufacturing, the province's big firms declined only 4%, while their counterparts in the rest of the country cut employment sharply (14%). The construction industry also enjoyed a boom in Ontario

through to the end of the 1980s, while it collapsed in the other provinces, producing a decline in big-firm employment of more than 40% over the decade to 1988. Much of the strength in construction had been concentrated in Alberta in 1978, especially in big firms, so the collapse of the Albertan construction market during the 1980s had a severe effect on national employment in big firms in this industry.

The other volatile industry is transportation, communications and utilities, where Ontario's employment declined significantly faster than it did in the rest of the country - 9% in the province, compared to 2% in the rest of Canada. This occurred principally because of cutbacks amounting to one-quarter of the work force in the big firms in the Ontario industry, compared to cutbacks half that big elsewhere.

The next two tables show the contribution to the total employment gain by each size category of each industry - Table 3.7 for Ontario and Table 3.8 for the rest of Canada. Among the interesting aspects of these tables:

- Small firms in personal and business services accounted for almost a fifth of all new jobs in Ontario. Since these firms employed only 7.5% of the province's labour force in 1978, this represents a remarkable contribution. One in seven of all new jobs between 1978 and 1988 came from firms in this industry employing fewer than 20 people.

- In the rest of Canada, small firms in personal and business services accounted for more than a quarter of all employment gains. Like Ontario, this was on a small base of only 8.2% of the labour force in 1978. Firms employing fewer than 20 people accounted for more than a fifth of all new jobs.

- Small manufacturing firms in Ontario accounted for 12% of all new jobs. Since these firms employed only 5.4% of the province's labour force in 1978, this, too, is a remarkable performance in an industry under extreme pressure. Medium-sized and big manufacturers lost the equivalent of 2.2% of the employment gains.

- Small manufacturing firms in the rest of Canada made a significant contribution to employment gains (9%), but their efforts were largely wiped out by the big manufacturing firms which lost the equivalent of 8% of the total job gains.

Table 3.7
Where the new jobs are - by size and industry - Ontario

Contribution to total job creation by each size category of each industry, 1978-88

Industry	**Contribution to job gains, by firm size (employees)**					
	0-19	**20-99**	**Small firms**	**100-499**	**500+**	**All firms**
	%	%	%	%	%	%
Primary	0.6	0.0	**0.6**	0.1	0.0	0.7
Mining	0.4	0.1	**0.5**	0.4	-1.0	-0.1
Manufacturing	8.6	3.5	**12.1**	1.2	-3.6	9.7
Construction	6.2	1.2	**7.4**	0.4	-0.2	7.6
Goods-producing	**15.8**	**4.8**	**20.6**	**2.1**	**-4.8**	**17.9**
Wholesale trade	4.9	1.0	**5.9**	0.9	-0.3	6.5
Retail trade	8.0	2.4	**10.4**	1.9	2.9	15.2
Trade	**12.9**	**3.4**	**16.3**	**2.8**	**2.6**	**21.8**
TC&U*	2.0	1.0	**3.0**	0.3	-5.7	-2.4
Finance, I&RE*	3.9	1.4	**5.3**	0.5	2.9	8.8
P&B services*	14.4	4.9	**19.3**	3.1	3.7	26.1
Market services	**20.3**	**7.3**	**27.6**	**3.9**	**0.9**	**32.5**
Community services	4.7	1.5	**6.2**	2.0	6.9	15.1
Public Administration	0.3	0.1	**0.4**	0.3	9.0	9.7
Funded services	**5.0**	**1.6**	**6.6**	**2.3**	**15.9**	**24.8**
Unclassified	2.1	0.6	**2.7**	0.4	0.0	3.1
ALL INDUSTRIES	**56.1**	**17.7**	**73.8**	**11.6**	**14.6**	**100.0**

**Notes: TC&U is Transportation, Communications and Utilities; Finance, I&RE is finance, insurance and real estate; P&B services is Personal and Business services; Community services includes education, health & welfare and cultural organizations.*

Table 3.8
Where the new jobs are - by size and industry - Rest of Canada

Percentage contribution to total job creation by each size of each industry, 1978-88

Industry	**0-19**	**20-99**	**Small firms**	**100-499**	**500+**	**All firms**
	Contribution to job gains, by firm size (employees)					
	%	%	%	%	%	%
Primary	2.8	-0.1	2.7	-0.2	0.1	2.6
Mining	1.9	0.4	2.3	0.1	-0.6	1.8
Manufacturing	9.0	0.2	9.2	-1.1	-6.9	1.2
Construction	6.7	-1.1	5.6	-0.9	-1.8	2.9
Goods-producing	**20.4**	**-0.6**	**19.8**	**-2.1**	**-9.2**	**8.5**
Wholesale trade	5.4	-0.3	5.1	0.2	-0.4	4.9
Retail trade	12.8	2.1	14.9	0.8	3.4	19.1
Trade	**18.2**	**1.8**	**20.0**	**1.0**	**3.0**	**24.0**
TC&U*	3.2	0.1	3.3	0.0	-3.9	-0.6
Finance, I&RE*	4.0	0.6	4.6	0.4	1.0	6.0
P&B services*	21.1	4.2	25.3	2.5	1.3	29.1
Market services	**28.3**	**4.9**	**33.2**	**2.9**	**-1.6**	**34.5**
Community services	8.2	3.2	11.4	5.6	4.9	21.9
Public Administration	0.7	0.3	1.0	0.4	6.4	7.8
Funded services	**8.9**	**3.5**	**12.4**	**6.0**	**11.3**	**29.7**
Unclassified	2.5	0.5	3.0	0.3	0.0	3.3
ALL INDUSTRIES	**78.3**	**10.1**	**88.4**	**8.1**	**3.5**	**100.0**

**Notes: TC&U is Transportation, Communications and Utilities; Finance, I&RE is finance, insurance and real estate; P&B services is Personal and Business services; Community services includes education, health & welfare and cultural organizations.*

- Retail trade was a more important job creator for the rest of Canada (15%) than it was for Ontario (10%).

- The rest of Canada seems to be building some momentum in personal and business services, because it did well in the firms employing 20 to 100 people and in the mid-sized firms employing 100 to 500 people. In these two size categories, personal and business services accounted for 4.2% and 2.5% respectively of all new jobs, compared to 4.9% and 3.1% in Ontario. Outside the funded sector, this was the best performance relative to Ontario and offers encouragement for the future.

- In Ontario, the mid-sized firms made positive contributions to job growth in every industry. In the rest of Canada, three made negative contributions in the goods-producing sector and the remainder, with the exception of community services and personal and business services, were virtually at a standstill.

Manufacturing

A closer examination of trends in manufacturing shows that Ontario's real strength lies in the diversity of its manufacturing industries, and the absence of weak industries among its bigger employers.

In Ontario, employment declined between 1978 and 1988 in only four of the 20 manufacturing industries, compared to 11 in the rest of Canada. Two of the industries which declined in Ontario were also major employers - primary metal and paper and allied products, which ranked as the seventh and eighth biggest employers respectively; between them, they lost the equivalent of 9.6% of the total employment gains.

In the rest of Canada, by contrast, the 11 declining industries included five of the top 10 employers. Paper and allied products and clothing, which rank third and fourth as employers, lost more jobs between them than the total new jobs created by the whole manufacturing sector between 1978 and 1988. Three other major employers - metal fabricating, primary metals and chemicals, ranked seventh to ninth - also lost jobs over the decade to 1988 in the rest of Canada. These percentages should be treated with caution; they appear excessively high because they are based on an extremely low number for the new jobs created by the manufacturers in the rest of Canada in the decade to 1988 - only 16,100, compared to Ontario's 1,048,200. But the industries that performed better didn't deliver spectacular results either. Only printing and publishing made a significant impact on employment.

Table 3.9
Ontario's manufacturing industries

Distribution of jobs created between 1978 and 1988 and of 1987 employment; and growth rates for small, big and all firms between 1978 and 1988. Ranked by contribution to job creation, Ontario.

	Industry shares of:		Industry growth rates in:		
Industry	**New jobs 1978-88**	**1987 Employment**	**small* firms**	**big* firms**	**all firms**
	%	%	%	%	%
Printing & publishing	18.1	7.8	74.5	22.2	39.9
Transportation equipment	14.9	15.4	155.6	5.2	13.7
Metal fabricating	11.2	9.7	75.8	-23.6	15.5
Furniture & fixtures	10.2	3.5	89.7	17.2	53.1
Chemicals	8.2	6.5	94.4	8.1	18.8
Rubber & plastics	8.1	4.9	139.3	-5.7	27.7
Electrical/electronic products	7.5	6.9	143.7	-2.8	15.1
Wood industries	7.5	2.9	85.3	0.0	42.7
Machinery	7.2	5.2	85.2	-9.1	19.6
Miscellaneous	6.4	4.8	66.4	-5.0	19.7
Food and beverage	6.0	10.1	52.6	-0.2	8.1
Clothing	2.3	3.0	57.8	-17.3	11.1
Non-metallic minerals	2.1	3.0	66.1	-4.8	9.8
Textiles	1.3	2.4	75.5	-9.8	6.7
Knitting mills	0.2	0.8	44.4	-8.1	3.8
Leather	0.1	1.2	26.7	-7.5	0.8
Petroleum & coal	-0.4	0.9	106.1	-9.6	-5.7
Tobacco products	-1.1	0.2	-50.0	-38.2	-38.9
Paper & allied products	-2.0	5.3	131.3	-16.9	-4.5
Primary metal	-7.6	5.7	70.3	-19.3	-14.5
TOTAL (%)	**100.0**	**100.0**	**83.9**	**-4.1**	**14.1**
TOTAL (000s)	**1,036.3**	**132.5**			

**Notes: In this table, big firms are those employing 100 or more people; small firms employ are those employing fewer than 100.*

The top five industries in Ontario as well as in the rest of Canada employ half their respective manufacturing work forces. They are:

Ontario	Rest of Canada
Transportation equipment	Food and beverage
Food and beverage	Wood industries
Metal fabricating	Paper and allied products
Printing and publishing	Clothing
Electrical/electronic products	Printing and publishing

In the rest of Canada, four of the top five are under pressure from international competition, the only one with really good prospects being printing and publishing. Ontario, by contrast, is strong in the automobile industry (which drives transportation equipment and metal fabricating), printing and publishing and the rapidly growing field of electrical and electronic products. The top five in Ontario employ 50% of the manufacturing work force and accounted for 57.7% of the new jobs between 1978 and 1988. The top five in the rest of Canada employed 50% of their work force and accounted for 41.1% of a very small growth in employment over the decade to 1988. Turning to growth rates, manufacturing in Ontario expanded over the decade to 1988 by 14%, compared to 1.5% in the rest of the country. These growth rates are lower than in other industries, of course, but the disparity between Ontario and the rest of the country is also greater in manufacturing than it is in most industries. (The other industries where the disparities were significant are construction, where employment growth was 65% in Ontario compared to 14% in the rest of Canada, and finance, insurance and real estate, where it was 52% compared to 22%.)

The remarkable aspect of Ontario's strength here is that the growth rate of small manufacturing firms was almost as high as the average for all small firms in all industries - 84% in manufacturing compared to 91% for all industries. In the rest of Canada, the small firms grew a lot faster than big firms, as might be expected, but they were still well below the average for all firms - 46% in manufacturing, compared to 63% in all industries.

Table 3.10
The rest of Canada's manufacturing industries

Distribution of jobs created between 1978 and 1988 and of 1987 employment; and growth rates for small, big and all firms between 1978 and 1988. Ranked by contribution to job creation, Rest of Canada.

Industry	**Industry shares of:** New jobs 1978-88	1987 Employment	**Industry growth rates in:** small* firms	big* firms	all firms
	%	%	%	%	%
Printing & publishing	99.4	7.1	45.0	13.8	27.6
Miscellaneous	63.8	3.7	70.1	-3.9	33.7
Rubber and plastics	55.2	3.3	97.2	10.0	33.1
Electrical/electronic products	52.1	3.7	111.3	5.8	25.0
Food & beverage	42.9	16.6	31.6	-3.0	4.1
Furniture & fixtures	32.5	3.1	60.1	-26.9	17.8
Transportation equipment	31.3	7.0	67.3	-3.5	6.6
Machinery	15.3	3.8	93.7	-39.0	6.0
Wood industries	4.3	9.6	36.5	-14.9	0.7
Knitting mills	-6.1	1.2	19.0	-18.9	-7.3
Chemicals	-8.0	4.1	87.3	-18.5	-2.7
Tobacco products	-12.0	0.4	-83.3	-35.7	-35.2
Metal fabricating	-13.5	6.9	36.9	-29.7	-2.8
Leather	-16.0	1.1	17.0	-37.0	-18.7
Petroleum & coal	-22.4	0.6	150.0	-38.0	-32.9
Primary metal	-36.2	4.7	50.0	-13.5	-10.0
Textiles	-38.7	3.5	34.4	-28.0	-14.6
Non-metallic minerals	-38.7	3.1	20.4	-32.3	-16.6
Paper & allied products	-50.3	9.5	87.0	-11.4	-7.4
Clothing	-55.2	7.2	18.5	-36.2	-10.7
TOTAL (%)	**100.0**	**100.0**	**45.9**	**-13.9**	**1.5**
TOTAL (000s)	**1,048.2**	**16.1**			

**Notes: In this table, big firms are those employing 100 or more people; small firms are those that employ fewer than 100.*

The three industries which grew the fastest were furniture and fixtures (53%), wood industries (43%) and printing and publishing (40%). In all three, small firms have a much greater share of employment than the average for all industries - 49%, 48% and 33% respectively, compared to a manufacturing average of 24%. Small firms in some of the other

industries grew even faster, however - transportation equipment (156%), electrical and electronic products (144%) and rubber and plastics (139%), in all of which small firms have a below-average share of the work force. This apparent aberration from the general rule that a larger presence of small firms usually brings more rapid growth to an industry is probably a result of unusual circumstances. It's reasonable to hypothesize that opportunities for small firms are beginning to appear more frequently because these industries have strong, but volatile, markets. In any event, the eight industries with the fastest growth rates have a significantly higher proportion of their employees in small firms. All but one had above-average representation in small firms, averaging 37% in 1987, while the remaining 12 industries had below-average representation in small firms, averaging 14%.

In the rest of Canada, the share of small-firm employment in the eight fastest growing industries was barely above the average of 30%, so the average for the remaining 12 was barely below the average for all industries. This is largely because two of the industries with high small-firm representation experienced a lot of difficulty in the period to 1988. Clothing and metal fabricating, both with more than 50% of employment in small firms, declined 11% and 3% respectively. Clothing, of course, has been subject to severe international competition, yet Ontario grew strongly by 11% over the period - a surprising result, since the province employed only 30,000 people in 1987, compared to 75,000 in the rest of country. Metal fabricating, on the other hand, reflects the general health of manufacturing, since it supplies all manufacturing industries, and the small firms in this industry grew only 37% in the rest of Canada, compared to 76% in Ontario.

Services

The funded and market sectors have contributed to job creation in almost exactly proportional terms, both in Ontario and the rest of Canada.

In Ontario, the market sector accounted for 59% of employment in the service industries in 1987 and for 57% of the jobs created between 1978 and 1988. As Table 3.11 shows, the situation is very similar in the rest of Canada, where the market sector is a slightly smaller part of the service industries than in Ontario (54%) and accounted for exactly the same share of employment growth (54%).

Table 3.11
Employment patterns in the service industries

Distribution of employment in 1987 and of employment gains between 1978 and 1988, between service industries. Ontario and the rest of Canada.

Industry	**1987 employment**		**Job gains, 1978-88**	
	Ontario	**Rest of Canada**	**Ontario**	**Rest of Canada**
	%	%	%	%
Transportation	6.3	7.4	2.2	-0.1
Storage	0.2	0.3	0.1	-0.2
Communications	3.6	3.8	-7.7	-0.4
Power, gas & water	2.4	1.6	1.3	-0.5
Finance companies	6.9	6.8	8.5	4.1
Insurance carriers	2.0	1.4	0.8	0.6
Ins. & RE agencies*	4.9	3.7	6.0	4.7
Amusement & recreation	2.0	1.8	2.4	3.2
Services to business	13.1	9.2	21.8	17.2
Personal services	2.1	2.1	3.0	4.3
Accommodation & food	11.3	11.9	11.6	14.4
Miscellaneous	4.0	3.6	6.8	6.3
Market services	**58.7**	**53.6**	**56.8**	**53.7**
Education	12.2	12.2	9.2	7.3
Health & welfare	13.1	15.9	16.5	25.9
Cultural organizations	0.6	0.6	0.6	0.9
Public Administration	15.5	17.8	17.0	12.2
Funded services	**41.3**	**46.4**	**43.2**	**46.3**
ALL SERVICES	**100.0**	**100.0**	**100.0**	**100.0**

**Notes: Insurance and real estate agencies*

The most impressive performance, as in previous years, came from services to business, which delivered a fifth of all the new jobs in the service industries - on the base of a 9.7% share of the employment in 1978. The industry thereby increased its share of service employment to 13%, while the rest of Canada expanded to a 9.7% share of employment in 1987 from 7.5% in 1978.

The other important contributor to job creation in Ontario was financial institutions, with 8.5% of the new jobs. Communications, on the other hand

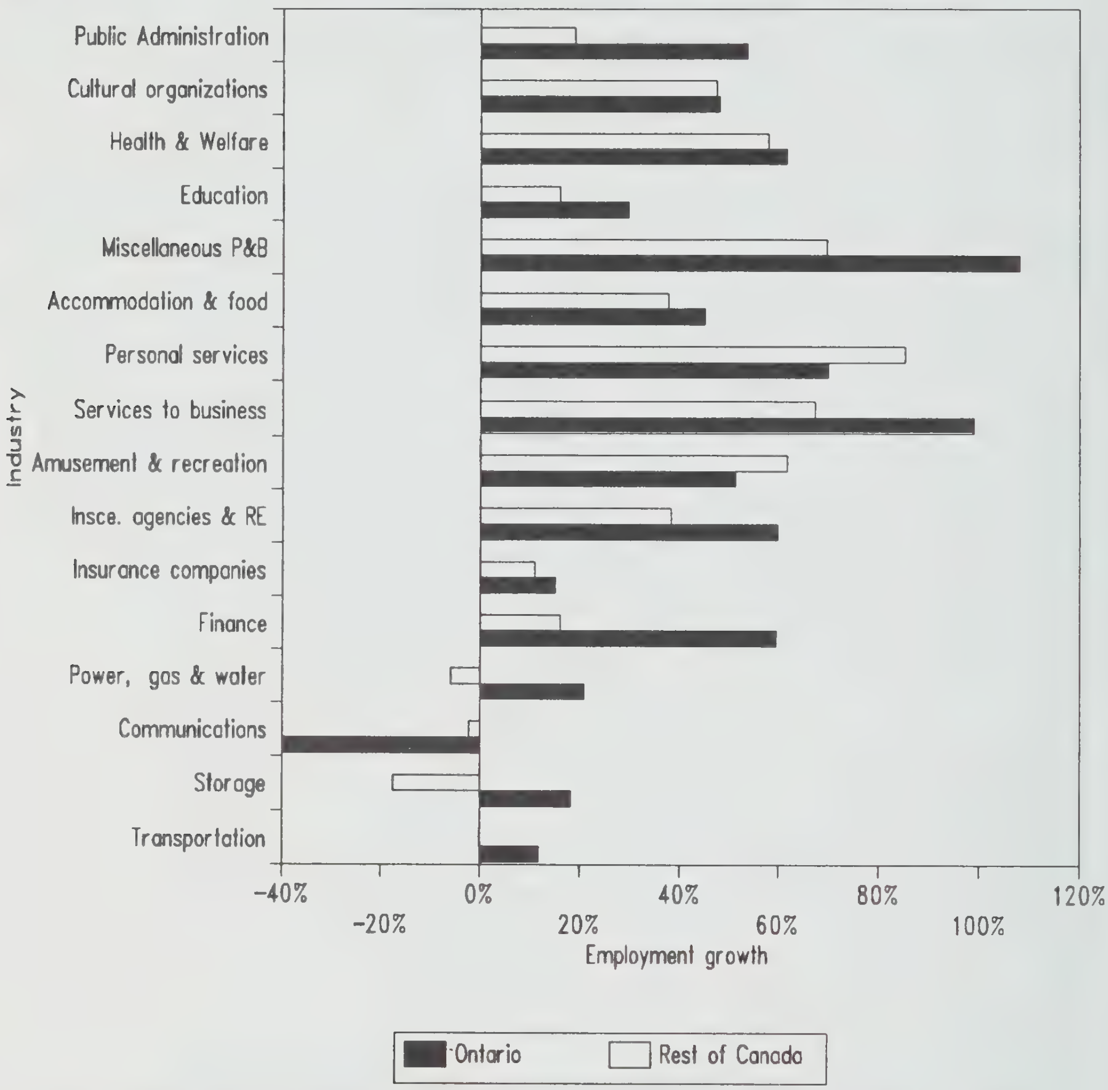
lost the equivalent of almost 8% of all new service jobs created between 1978 and 1988. These deep cuts in employment, unmatched elsewhere in the country, were probably due to the telephone companies slimming down in the face of deregulation - the decline was entirely limited to companies employing more than 500 people, and smaller companies all grew strongly, presumably because they were able to pick up the slack and exploit new opportunities.

The only major difference between Ontario and the rest of the country lies in the funded sector, where the other provinces have a bigger contingent in both public administration and health and welfare. These two balanced each other out over the decade to 1988, because public administration was slowing down its growth, while health and welfare was accelerating.

The growth rates of individual industries were generally higher in Ontario than elsewhere, as Chart 3.7 shows. The major areas of strength for Ontario were miscellaneous services and services to business, which doubled over the decade to 1988. The next best, with growth of 70%, was personal services, which was the best performer for the rest of Canada, with a growth rate of 85%.

Chart 3.7
A decade's growth in employment in the service industries

Employment growth, 1978-88, by industry, for Ontario and the rest of Canada



As might be expected, small firms grew most rapidly in the service industries. Less expected, however, is that small firms in the industries most heavily dominated by big firms grew the fastest. As Table 3.12 shows, the highest growth rates in small firms were in financial companies, where small firms accounted for only 7% of total service employment in 1987, and in communications, where they accounted for less than 4%. These are both fast-paced industries that offer lots of opportunities, so they

are well suited to small firms. The problems encountered by big firms in these industries have also created many market niches for agile, small firms.

Table 3.12
Growth patterns in the service industries

Employment growth rates, 1978-88, for small* and big* enterprises in Ontario and the rest of Canada.

	Ontario		Rest of Canada	
Industry	**Small firms**	**Big firms**	**Small firms**	**Big firms**
	%	%	%	%
Transportation	82.2	-13.4	41.3	-16.7
Storage	82.4	-22.2	36.0	-31.6
Communications	178.1	-44.8	97.1	-7.1
Power, gas & water	53.3	17.4	77.5	-11.1
Finance companies	229.4	39.1	75.4	6.1
Insurance carriers	94.1	11.9	66.7	8.6
Ins. & RE agencies*	89.9	10.7	53.6	10.0
Amusement & recreation	62.8	31.6	64.7	55.1
Services to business	148.1	60.7	112.1	21.9
Personal services	75.7	51.3	91.2	51.5
Accommodation & food	67.3	15.5	54.7	6.3
Miscellaneous	129.5	69.8	86.7	34.5
Market services	**99.3**	**9.6**	**69.6**	**1.8**
Education	109.6	25.7	82.2	10.6
Health & welfare	130.2	38.8	122.7	35.4
Cultural organizations	50.0	33.3	48.4	30.0
Public Administration	44.4	54.2	50.0	17.3
Funded services	**106.5**	**39.7**	**97.4**	**19.6**
ALL SERVICES	**100.6**	**23.9**	**75.5**	**11.7**

**Notes: Insurance and real estate agencies. For the purposes of this table, big firms are defined as those employing 100 or more people.*

If the performance of all the service industries is separated into small-business dominated and big-business dominated sectors, small firms in Ontario did better in the industries dominated by big firms than they did in those dominated by small firms - growing 114% in the former, compared

with 95% in small-firm dominated industries. Big firms in industries dominated by big firms, by contrast, grew at half the rate of those in industries dominated by small firms - 21% compared with 37% in small-firm dominated industries. The contrast in performance of big firms is even more pronounced in the big-firm dominated part of the market sector, where small firms grew 115% and big firms declined 6.5%. The big firms did best in services to business, personal services (where small firms account for 76% of employment) and miscellaneous. Big organizations in Ontario also did well in public administration, where employment increased by more than 50% over the decade to 1988.

The patterns were similar in the rest of Canada, at a slightly lower rate. The major exception was amusement and recreation, where big firms performed almost as well as small firms, expanding 55%.

Average salaries

When salaries are added to the equation of job creation, Ontario still comes off better than the rest of Canada, but small firms don't look as good. Average salaries paid in the four main sectors vary quite significantly, as Chart 3.8[9] shows. Trade was the sector with the lowest salaries in Ontario in 1987, averaging $16,548 for all companies, compared with $24,072 in the goods-producing sector.

In the rest of Canada, salaries averaged about 88% of Ontario's, with the greatest disparities in the goods-producing industries (85%) and market services (86%). In funded services, salaries in the rest of Canada were 93% of Ontario's.

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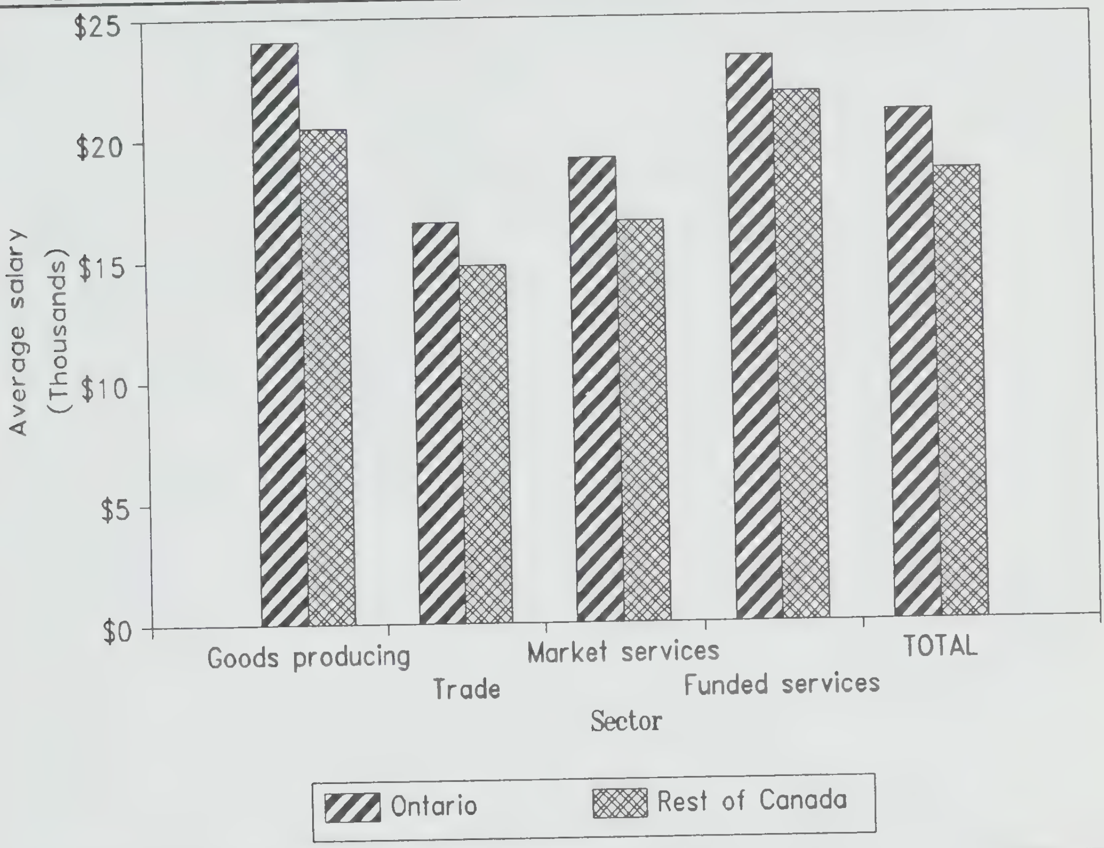
[9]Source: Statistics Canada, Small Business & Special Surveys Division. These statistics are developed differently from those used earlier and in chapter 2. In the balance of this chapter, employment is defined by the concept of "individual labour units", which count every person (part-time, full-time or on overtime) as a single worker. In the statistics used earlier, employment statistics are based on "average labour units", which provide employment statistics equivalent to the number of full-year workers, counting a part-time worker as a fraction of a full-time worker.

Chart 3.8
Salaries are higher in Ontario

Average salaries, by sector, Ontario and the rest of Canada, 1987



When average salaries are analyzed by firm size, the differences become more significant. The smallest firms, employing fewer than five people, pay their employees about 40% of the salaries offered by firms with more than 500 employees. Firms with fewer than 20 employees pay at about 60% of the rate in the big firms. As Table 3.13 shows, this applies even in the funded sector, which implies that the main reason for the "low" salaries is that many of the workers in these small organizations are part-time. Many are also startups, in which salaries are often much lower until the business is established.

The only exception to the rising pay in bigger companies is in trade, where firms with more than 500 employees pay salaries at about 70% of the level of firms with 100 to 500 employees.

Table 3.13
How salaries compare in different sized firms

Payroll divided by individual labour units, by sector and firm size, Ontario, 1987

	Average salaries for firms employing:					
Sector	**1-4**	**5-19**	**20-49**	**50-99**	**100-499**	**500+**
	$	**$**	**$**	**$**	**$**	**$**
Goods-producing	10,728	17,727	21,638	23,270	24,838	30,194
Trade	9,967	15,525	18,749	21,073	22,348	15,659
Market services	11,152	13,776	15,276	17,738	20,571	24,727
Funded services	12,061	13,580	14,074	15,622	19,270	25,848
All sectors	**10,774**	**15,368**	**18,082**	**20,293**	**22,372**	**25,528**

It is also notable that average salaries in big firms in the goods-producing sector are the highest of all, at $30,194, or 20% higher than $25,848 in funded services and $24,727 in market services. In smaller companies, the margin is even bigger, at more than 30% in firms with five to 99 employees. In firms with 5-499 employees, trade pays better than all the other service industries.

These divergences produce some interesting effects on the distribution of payrolls between firms of different sizes in the same sector. As Table 3.14 shows, small firms generate 31% of the payroll in the goods-producing sector with 41% of the employees. Surprisingly, the imbalance is just as severe in market services, where small firms account for 34% of the payroll with 47% of the employees. There is relatively little imbalance in trade, however, which is also the sector where mid-sized firms generate the highest earnings relative to their employment.

Table 3.14
Sectoral distribution of payroll and employment

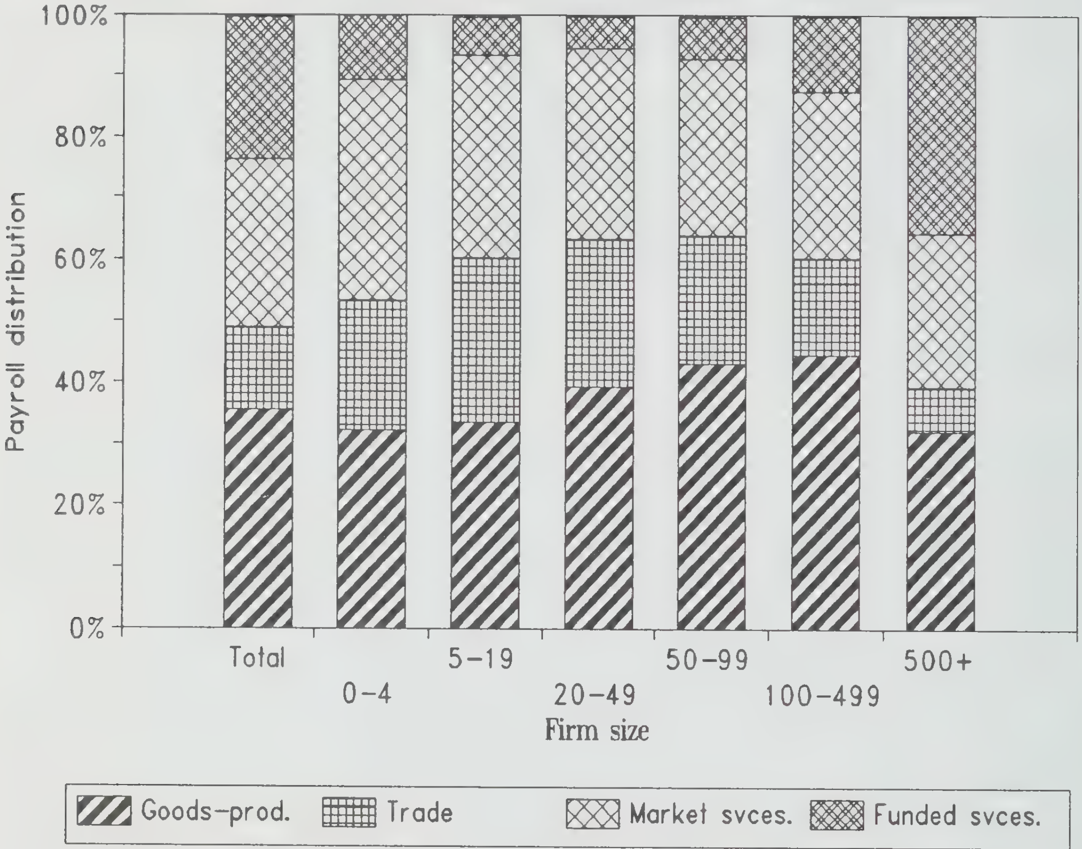
Share of total payroll and employment, by number of employees per firm within sectors, Ontario, 1987

	Distribution, by firm size within sectors, of:					
	payroll			**employment**		
Sector	**1-99**	**100-499**	**500+**	**1-99**	**100-499**	**500+**
	%	%	%	%	%	%
Goods-producing	30.6	19.3	49.9	41.2	18.7	39.8
Trade	51.9	18.1	29.9	54.9	13.4	31.6
Market services	34.4	15.2	50.3	46.8	14.1	39.0
Funded services	8.8	8.1	82.9	15.1	9.8	74.9
All sectors	**29.6**	**15.3**	**55.0**	**40.0**	**14.4**	**45.4**

Finally, the imbalances in salaries also lead to quite different sectoral profiles of different sizes of firms. As Chart 3.9 shows, big firms are heavily concentrated in funded services, which account for 36% of the earnings of firms that size. In other firm sizes, funded services account for 5%-12%. Small firms are weighted heavily toward market services, which account for about a third of the earnings of firms with fewer than 50 employees, compared to about a quarter in all larger firms. The goods-producing sector accounts for the highest share of earnings in the mid-sized and large-small firms, where it averaged about 43%, compared to a third in the firms with fewer than 20 or more than 500 employees.

Chart 3.9
Sectoral concentration in each size of firm

Distribution of payroll by sector, within each size of firm, Ontario, 1987



Part II

Perspectives on Entrepreneurs

Three studies published in 1990 have deepened understanding of entrepreneurs in Ontario. The first examined family businesses, the second Franco-Ontarian entrepreneurs, and the third studied early-stage financing by informal and formal venture capitalists.

CHAPTER 4
FAMILY-OWNED BUSINESSES

In 1987, there were about 167,000 Canadian-controlled private corporations (CCPCs) in Ontario and 70% of them were family-owned, according to a recent survey[1]. As Table 4.1 shows, the distribution of the family-owned firms by their annual sales was remarkably close to the distribution by size for all firms.

Table 4.1
The weight of family-owned firms in Ontario

Number and percentage distribution of Canadian-controlled private corporations, by family ownership and non-family ownership, 1987

Sales range	Non-family owned		Family owned		Total	
$million		%		%		%
.025 - .25	25,924	15.5	57,819	34.7	83,743	50.2
.25 - 2	19,461	11.6	47,709	28.6	67,170	40.2
2 - 5	3,320	2.0	6,757	4.0	10,077	6.0
5 - 10	988	0.6	2,501	1.5	3,489	2.1
10 - 50	791	0.5	1,681	1.0	2,472	1.5
TOTAL	**50,484**	**30.2**	**116,467**	**69.8**	**166,951**	**100.0**

The definition of family-owned, however, is not as straightforward as might be supposed. In a recent survey of CCPCs, there were 120 owners who said they did not have a family-owned corporation, but almost half of them (59) also said that family members owned shares in the business; fully 91% of them (109) said family members worked in the business. At the other extreme, are the entrepreneurs who described their business as family-owned but no-one in the family worked in the business (42 people said this)

[1]Source: *Survey of Family-owned Business*, conducted by Statistics Canada and sponsored by Industry, Science & Technology Canada; the Ontario Ministry of Industry, Trade & Technology; the Saskatchewan Ministry of Economic Development and Tourism; and the Canadian Association of Family Enterprise, 1990.

or owned shares (130). The study concluded that "family-owned" means a business that the owner says is family-owned *or* that employs family members *or* that has other family members as shareholders. In fact, all but 7% of the respondents in the survey said that family members worked in their businesses. Almost three-quarters have family members who both own shares in the business and work there.

The study was limited to Canadian-controlled private corporations, which Revenue Canada defines as private corporations resident and incorporated in Canada, that are not controlled, directly or indirectly, by non-residents or by public corporations. In 1987, there were about 137,000 firms in Ontario that were not CCPCs - mostly unincorporated businesses, but also foreign-controlled firms and public companies. Since many of the unincorporated businesses are also family-owned, it is probably safe to say that family-owned businesses account for more than half of all the firms in Ontario.

The distribution of family-owned firms between industries differs somewhat from that of all firms, but family-owned firms have clearly penetrated all industries, as Table 4.2 shows. The family firms are heavily concentrated in finance, insurance and real estate, but somewhat underrepresented in accommodation services.

Table 4.2
Family-owned firms are in every industry

Distribution by industry of family-owned and all businesses, 1987

Industry	Family businesses	All businesses
	%	%
Primary	4.0	5.4
Manufacturing	7.8	7.4
Construction, Transportation, Communications & Utilities	20.8	15.4
Wholesale trade	10.2	6.2
Retail trade	19.0	14.6
Finance, Insurance & Real estate	22.8	6.6
Government services	1.0	0.4
Accommodation services	14.4	25.7
Other		19.3
TOTAL	**100.0**	**100.0**

In terms of the larger sectors, 43% are in services, 29% are in trade and 27% are in goods-producing industries.

There are larger differences in the relative weights of other financial assets, however, as Table 4.3 shows.

Table 4.3
Family-owned firms have stronger financial statements

Share of total assets, equity and profits of Canadian-controlled private corporations held by family-owned firms, 1987

Sales range	**Assets**	**Equity**	**Profit**
$ million	**%**	**%**	**%**
.025 - .25	8.5	13.6	10.9
.25 - 2	18.8	24.5	34.5
2 - 5	10.2	10.7	12.2
5 - 10	8.2	8.2	7.1
10 - 50	19.3	19.5	12.3
TOTAL	**65.0**	**76.5**	**77.0**

Family-owned firms appear to be more effective in running their businesses. They have a smaller share of total assets (65%) than their 70% share of number of firms and of total sales, yet they have a larger share of equity (76%) and profits (77%), indicating that non-family owned firms have a smaller than proportionate share of these items. Family owned firms are less leveraged than the others and they earn a higher return on their assets.

Among the other conclusions reached by the survey:

- Family-owned firms grew at an average annual rate of 13.1% between 1984 and 1987, somewhat faster than non-family owned businesses, which grew at 9.4% a year. The average for all CCPCs was 12.3% a year.
- 90% of the sample in the survey had sales of less than $2 million.
- 57% of the sample were first-generation businesses. Only 8% were in the third generation or more.

Some of the more surprising responses concerned the attitude of owners toward succession, which is acknowledged by experts as the single biggest problem in family-owned businesses (and perhaps the reason why so few family businesses last beyond the first generation). Only 12% of the sample thought that succession was a challenge for their businesses. 40% of the

respondents did not know if succession was a problem and, of the 60% who did know, more than half thought it would not be a problem for at least 10 years.

Asked what they considered to be the biggest challenge they face, 27% of the respondents in this survey answered management and organization. The ranking for all the perceived challenges was:

Management	27%
Growth and diversification strategy	17%
Financing	16%
Succession	12%
Capital gains	9%
Motivating and educating family	5%

The final question asked was what the owners considered would most help their firm to grow. Their rankings were:

Acquiring new technology	50%
Marketing in Canada	47%
New product development	41%
Automating production	33%
Forming partnerships	32%
Exporting to the U.S.	30%

CHAPTER 5
FRANCO-ONTARIO'S SMALL BUSINESSES

Francophone entrepreneurs in Ontario have not generally enjoyed a high profile, but in the areas of the province where French is widely spoken, they have built successful businesses that operate to a significant degree in the French language. To identify these businesses and paint a profile of their operations, the Ministry of Industry, Trade & Technology conducted a study of Francophone small businesses in the province[1].

More than 700 eligible responses were obtained in personal interviews and it materialized that the age and gender distributions of the francophone entrepreneurs are not that different from those of the general population of entrepreneurs in Ontario. As Table 5.1 shows, however, there are a number of variations in the profiles of the average Francophone and Ontarian. It may be that the sample was not entirely representative of all Franco-Ontarian entrepreneurs, because the names in the survey were drawn from lists of association members and referrals (unavoidable in a pioneering study). This sample is more typical of a survey of successful firms, in which young firms are underrepresented.

The Francophone firms in this study were generally older and more established than the general population of small firms in Ontario. The average period for which all businesses in Ontario have been operating is nine years, compared to almost 16 years for the Francophones in this sample. Indeed 85% of the Francophones have been in business for more than five years. Their average sales are more than four times as big and their startup investment was generally higher. It is interesting to note, however, that 56% of the Francophones' investments at startup were less than $30,000 (or $54,000 in 1990 dollars), which is comparable to the most recent study[2] of startups, in which 49% of the firms had startup investments of less than $50,000.

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[1]Source: Study on Franco-Ontarian Small Businesses, prepared by Rhéal Leroux & Associates for the Ministry of Industry, Trade & Technology, 1990.

[2]Source: Newly-formed small businesses in Ontario, 1982-87, prepared for the Ministry of Industry, Trade & Technology by Laventhol & Horwath. 1988.

Consistent with the higher startup investments, two thirds of the Francophone firms were incorporated, compared to a third in the whole province. Since most firms don't incorporate until they have become established, a low proportion of unincorporated firms usually means there are fewer young firms than usual. In fact, the average Francophone firm had been in business for 16 years but incorporated for only 12, indicating that, on average, they incorporated four years after opening their doors.

Table 5.1[3]
Profile of Franco-Ontarian businesses

Comparison of key elements in the profiles of Franco-Ontarian entrepreneurs and all entrepreneurs in Ontario

	Franco-Ontarian entrepreneurs	All entrepreneurs in Ontario[4]
Proportion of males	76%	76%
Average age	47	44
Proportion with incorporated businesses	65%	32%
Number of employees	12	*13
Period since startup	15.8 years	**8.9 years
Average startup investment	$117,000	$103,000
Average startup investment (1990 dollars)	$210,000	$155,000
Portion of investment provided by owner	70%	30%
Annual sales	$1,072,000	○$233,000
Growth rate in annual sales, 1987-89	15% p.a.	n/a
Expected sales growth, 1990-92	17% p.a.	n/a

Notes * *Average number in market sector only. In the rest of Canada, the average is 9.*

** *The average age of businesses in Ontario was calculated on the basis of a model developed from a special run of Employment Dynamics, showing failures by year of startup (see Chapter 2, Births, Deaths and Survivors).*

○ *Only incorporated businesses, 1987.*

There is a heavy weighting in this sample of firms based in Eastern Ontario. This does not pose problems for the conclusions, but it does limit the scope for regional comparisons. In general, the sample covers all the

[3]Source: Ibid. *Study on Franco-Ontarian Small Businesses*

[4]Sources: 1986 census; Employment Dynamics provided by the Small Business and Special Surveys Division of Statistics Canada; and *Newly-formed small businesses in Ontario, 1982-87.*

main sectors in proportions comparable to the province as a whole and can be considered a good cross-section of the Francophone small-business community.

Some of the main conclusions to come from the study are as follows:

- Only 8% of the firms export their products or services and 71% of these firms concentrate on the U.S. The next most important destination for exports is France, with 7%.
- The average length of schooling is 12 years, with a tenth having less than grade 9 and a quarter having a university education. This pattern is skewed at both ends of the spectrum, as is the profile of all entrepreneurs in the province, but these Francophones are better educated than average, 15% of whom have less than grade 9 and 20% of whom have a degree.
- Francophone small firms, like their Anglophone counterparts, are generally unfamiliar with government programs. The most widely recognized program is Ontario Summer Employment, which is known to a quarter of the firms. Five programs accounted for about 80% of the usage of government assistance - Ontario Summer Employment (32%), Futures (24%), Advisory programs (8%), Ontario Skills Development (8%) and the financial services of the Federal Business Development Bank (7½%). The users of these programs were well satisfied with the result, giving them an approval rating of 7½ on a scale on one to 10.

The major problems faced by the Francophone firms were, in order of importance:

Recruitment of skilled labour,
Payroll taxes,
Government regulations and bureaucracy,
Lack of subsidies,
Energy and fuel costs, and
Financing and cash flow.

Other problems identified by the study include the size of the market, competition, the state of the economy (particularly interest rates), irregularity and uncertainty of contracts, insurance costs, financing clients, the cost of modern equipment and the cost of bilingualism.

A fuller discussion of the language issue and employment challenges follows.

Language

French is used as the working language by slightly more than half the companies in this study. As Table 5.2 shows, however, this is weighted somewhat toward internal communications with employees.

Table 5.2[5]
The use of French in the workplace

Percentage of small Francophone firms using French in communications, internally and externally.

	English	French
	%	%
Employees	33.1	66.9
Financial institutions	45.0	55.0
Municipal governments	47.3	52.7
Clients	50.4	49.6
Suppliers	56.3	43.7
Government of Ontario	60.7	39.3
AVERAGE	**48.8**	**51.2**

Almost half the firms used French in more than 90% of their communications with their employees, while 13% used English almost entirely. Similar polarization is found in communications with municipalities, where 35% use French only and 28% use English almost exclusively; also 17% use French almost exclusively in their dealings with the provincial government, compared with 35% who use English exclusively.

The main reason why these French-speaking entrepreneurs do not use their own language more in the workplace is "out of respect for Anglophone clientele," a reason cited by almost 40% of the respondents. Strangely, the second most common reason was "no particular reason" and the third "clientele is bilingual." Slightly more than 5% said the major constraint on their use of French is "we live in Ontario."

In view of these perceived constraints, it is perhaps not surprising that only 42% of Francophone entrepreneurs use French in public relations. This applies consistently to all the major vehicles for public relations - signage, stationery, publicity and business cards.

[5]Source: Ibid.

Employment practices

The firms in this survey employ a total of 7,724 employees, 71% of whom are Francophones. When it comes to their perspective on the challenge of finding good employees, however, the Francophones are no different from their Anglophone counterpart: 65% of them said the greatest difficulty they face is finding good skilled workers. The firms complaining of difficulties in recruiting employees were most in evidence in services to business, followed by wholesale trade and finance, insurance and real estate. As Table 5.3 shows, in all the other industries, a little fewer than 50% are experiencing recruitment difficulties.

Table 5.3[6]
The incidence of employee problems

Percentage of the Francophone firms that reported having difficulty with recruiting good personnel and retaining them, by industry.

Industry	Firms having problems recruiting %	Firms having problems with turnover %
Services to business	60.0	15.7
Wholesale trade	51.2	16.3
Finance, Insurance & Real Estate	50.0	21.3
Retail trade	49.2	20.3
Manufacturing	46.5	20.3
Personal and community services	44.1	18.0
Construction	41.9	14.3
Transport, Communications & Utilities	40.0	8.3
Primary	25.0	9.1
Other	51.6	30.0
AVERAGE	**47.0**	**18.0**

Once these Francophone entrepreneurs have found good employees, they usually manage to hang on to them, but there are still 18% who have problems with excessive turnover. Again, this problem is most acute with skilled workers, who represent the main difficulty for more than half those who have a turnover problem. Language does not appear to be a major factor in the retention of good employees.

[6] *Source: Ibid.*

As is the case with most small firms, the Francophone small businesses did not spend a lot of time and money sending their employees on formal courses. For the most part, training in small business is on the job. Nonetheless, almost half (48%) of the employees in this sample of firms attended training sessions outside the company. For most of them, however, the benefits were not widely spread, as almost two thirds of the firms sent fewer than 10% of their employees on courses. A little more than 15% sent at least 30% of their employees on courses. The three industries that are most enthusiastic about sending their employees on courses are also the three with the worst recruitment problems - services to business (72%), finance, insurance and real estate (71%) and transportation, communications and utilities (61%).

CHAPTER 6
EARLY-STAGE FINANCING

In the second half of the 1980s, Canada enjoyed a high international ranking in terms of investments made in early-stage firms by its venture capital firms. This superficially healthy situation, however, conceals a sharp reduction in activity in the private-sector funds, and a compensating surge in investments by public-sector funds. Although venture capital funds provide a small share of new-venture financing (especially compared to informal investors), they are still important players, as much for the tone they set as for the amounts they invest. In 1988 and 1989, about $75 million was invested by private and public funds, close to the U.S. in proportional terms and lagging only Spain, which had a very strong showing, as Table 6.1 shows.

Table 6.1[1]
How Canada's venture capitalists compare internationally

Ranking of the major countries by money invested in early-stage ventures by the venture-capital funds, 1988.

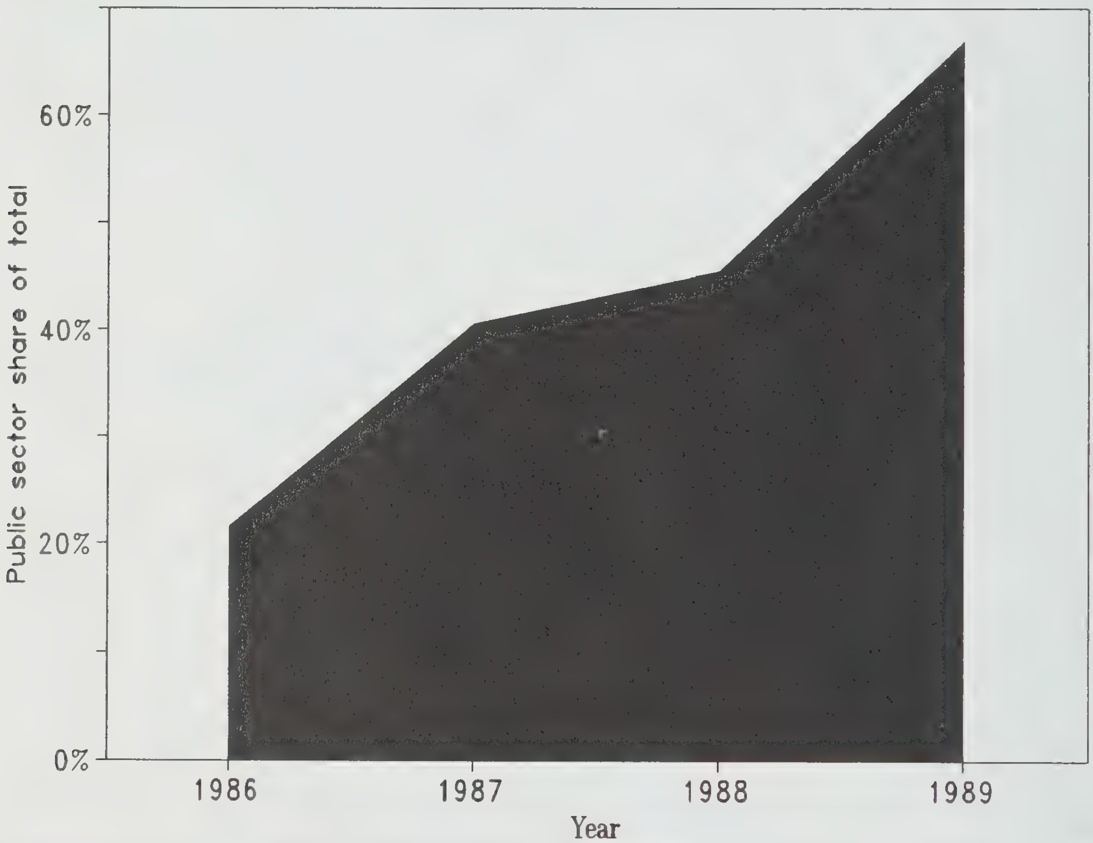
Country	Investments in early-stage deals	% of all venture capital deals	Number of early-stage deals	% of all venture capital deals
	US$ millions	%		%
U.S.	732	24	402	30
Britain	200	10	560	27
France	110	17	368	28
Canada	**65**	**22**	**122**	**45**
Spain	36	40	59	52
Netherlands	25	16	205	30
West Germany	15	14	67	30
Belgium	13	17	31	25

[1]Source: Unless otherwise noted, all the data in this chapter is drawn from *Financing Early Stage Companies*, a study prepared by Venture Economics Canada for the federal and Ontario governments and other provincial agencies. 1990. For information about Ontario government financing programs, see Chapter 7.

However, 24 Canadian investing groups (about half of the firms who made early-stage investments during this period) left the early-stage financing market between 1986 and 1989. The gap was filled by public sector funds, which greatly increased their share of the market, from 21.5% in 1986 to 66.8% in 1989, as Chart 6.1 shows.

Chart 6.1
The public sector has become the main source of venture capital for early-stage firms

Share of the public-sector funds in the total early-stage investments made by venture capital firms in Canadian businesses between 1986 and 1989

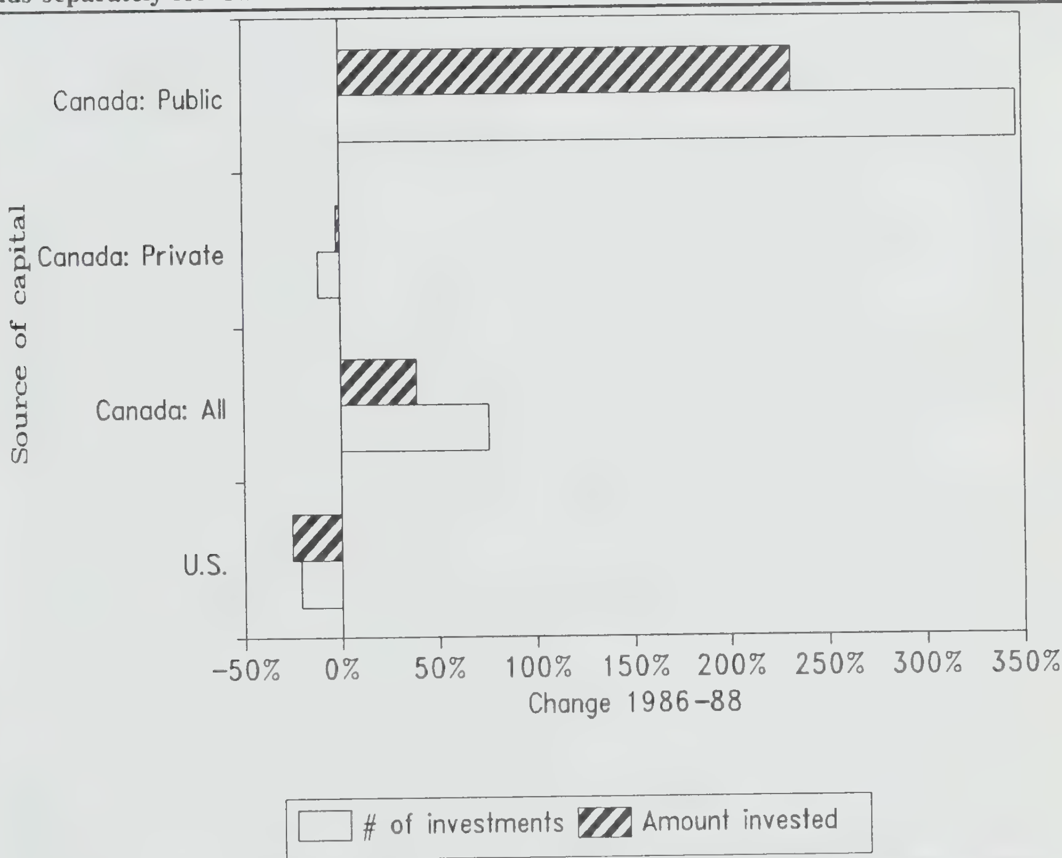


The withdrawal from the market by private-sector funds has led to the perception among entrepreneurs in Canada that venture financing is unnecessarily scarce, particularly compared with the U.S. The people who control the private-sector venture capital funds, on the other hand, see the Canadian market as limited and unprofitable, partly because they feel the entrepreneurs have insufficient managerial expertise, partly because the

deals are too small to make it worth their while to invest the necessary amount of their own time in each deal. The private-sector investors perceive the situation as "too much money chasing too few deals" because the supply of capital is strong despite their scepticism of the value of investments in Canada. As Chart 6.2 shows, the early-stage financings in the private sector have actually decreased, while those in the public sector have soared.

Chart 6.2
Private-sector funding of early-stage firms is stagnant or declining

Percentage increase over the two years to 1988 of early-stage investments, by number and amount, by venture capital firms in the U.S. and Canada, showing public and private-sector funds separately for Canada



It is noteworthy that Canadian venture capitalists were not alone in their perception. Early-stage financings in the U.S. also declined over the period - and the declines in the Canadian private sector would have been almost identical had it not been for one very large deal.

The average size of these investments was about $800,000 in 1989 and $620,000 the year before, which is significantly below levels associated with private-sector venture capitalists, who would normally average more than $1 million in their deals. This illustrates that public-sector funds are more likely to invest in early-stage financings than their counterparts in the private sector. For the purposes of this study, early-stage financings are defined in four categories:

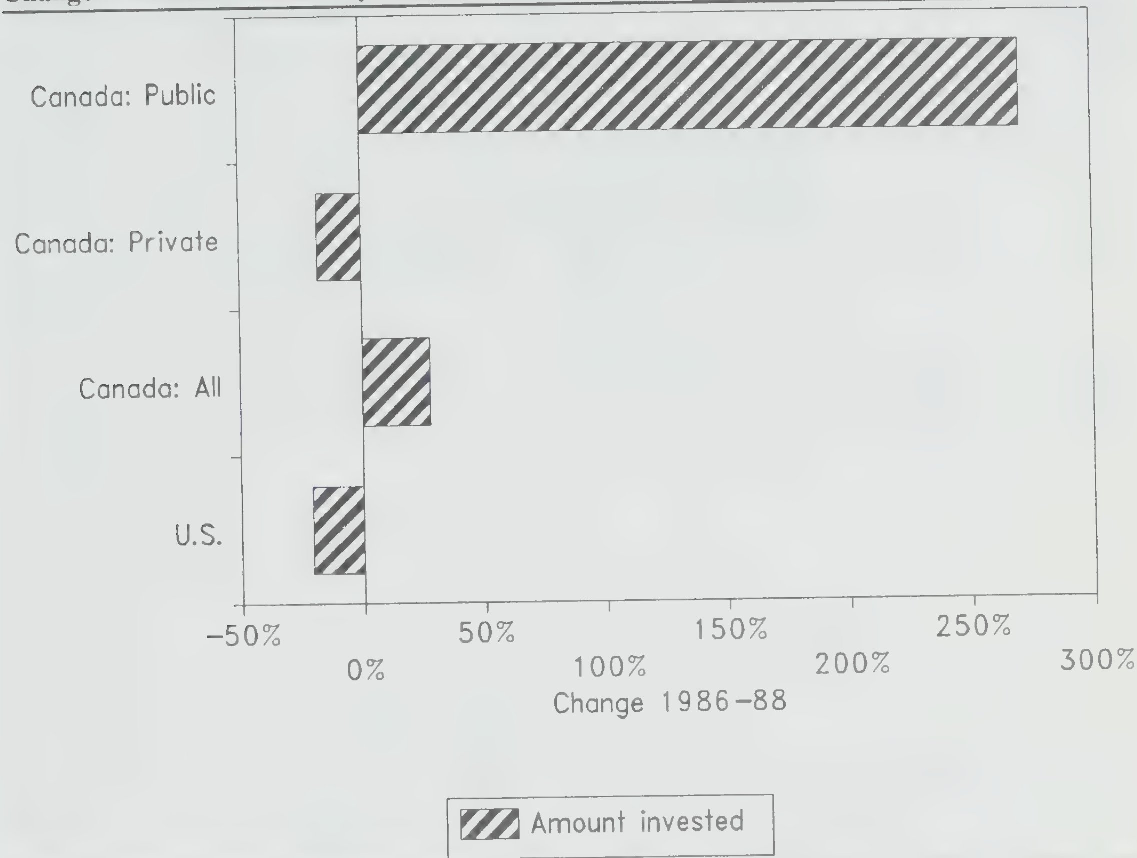
- *Seed financing* is provided to prove a concept;
- *Startup financing* is aimed at product development and initial marketing, usually with the management team partly in place;
- *First-stage expansion financing* is for companies that have spent their startup funds and need funds to start commercial manufacturing and sales; and
- *Re-startup financing*, rarely used in Canada, is intended to restructure a company that has failed in its first attempt to grow.

Many of the departing firms in the private sector are based in Ontario. This makes it difficult for public-sector funds in the province which try to piggy-back investments by the private sector, a technique which ensures the investment judgements will continue to be made by the private sector. In the country as a whole, the estimated amount of capital available among formal venture-capital firms that invest in early-stage companies is about $600 million. However, this money is not being invested to a great extent in the early stage companies, partly because a large percentage of the funds are in huge funds like Alberta's Vencap Equities and Solidarity Fund, which do not favour early-stage financings.

The decline in private-sector interest and the arrival of public-sector funds was mirrored in the technology industries (communications, computer hardware, computer software, other electronics, biotechnology and medical/health related companies). These were, for a while, the darlings of the venture-capital industry, because they offered the best hope for spectacular returns, but venture capitalists on both sides of the border became disenchanted in the mid-1980s, when it became apparent they were maturing more slowly than the investors had hoped. As Chart 6.3 shows, private-sector commitments of funds to early-stage ventures declined by 18% between 1986 and 1988, compared to a decline of 20% in the U.S. The public sector increased the number of its technology investments to 52 from six, and the amount invested to $22 million from $6 million.

Chart 6.3
Technology firms face declining interest from venture capitalists

Change in amount invested by venture capital firms in technology-based firms, 1986-88.

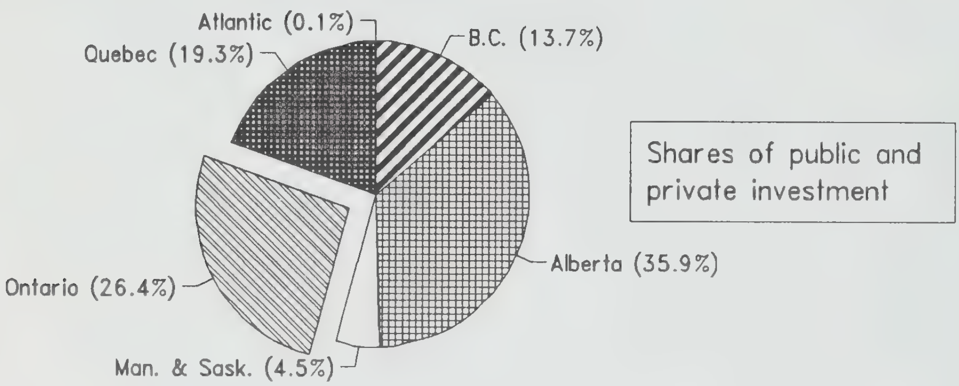


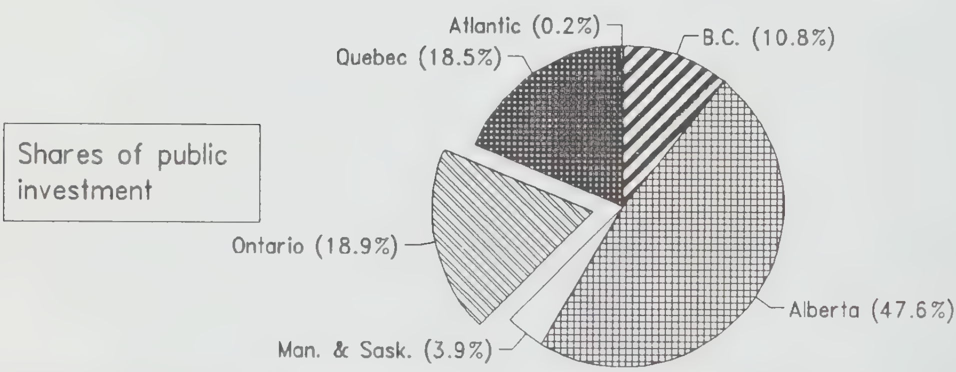
Much of the growth in public-sector venture capital was in two provinces - Quebec and Alberta. As Chart 6.4 shows, Alberta accounted for almost half of all public-sector financings of early-stage companies in 1986-89. Ontario accounted for only 19%. Ontario receives less than its proportional share of early-stage financings, with only 26% of the total, while the Atlantic provinces received almost nothing during this period.

Meanwhile, the private-sector venture capitalists redirected much of their attention to U.S. ventures, which attracted 23% of the funds committed by the private-sector funds during the period 1986-89.

Chart 6.4
Provincial shares of venture capital investments

Provincial share of total funds invested by venture capital companies in 1986-89 and shares of investments by public-sector venture capital funds.





The role of the public sector has been critical in filling the gap left by the departure of private-sector funds. This is particularly true for the smaller deals, in which the private sector finds it difficult to make a profit. But the public sector faces other constraints, not the least of which is budget deficits, and it remains critical that the private sector return to the market, even if only because these funds bring an important discipline to bear on both investors and entrepreneurs.

The Informal Investor

The venture capital industry has never been the only source of venture financing, however. Entrepreneurs starting their own companies have relied for many years on informal investors - their friends and relatives and the local "angels" who have some money to invest and enjoy the challenge of being associated with high-risk ventures. In a recent survey of informal investors[2], it was found that informal investors have significant amounts of capital, which they invest consistently, year after year. They invest in all regions, and, because they are builders of businesses themselves, are able to provide management assistance, the critical element of successful venture investing.

These investors operate independently of the formal venture capitalists, with whom they maintain very weak links. That may be because they are very different people. The informal investors are generally owner-operators themselves:

- 52% were business owners;
- 75% had founded businesses;
- 62% had family income of more than $100,000 a year;
- 52% had a family net worth of more than $1 million (a third were worth more than $2 million); and
- 71% had university or college degrees.

Almost half the informal investors already knew the management of the firm in which they were investing when they negotiated the deal. The investors were friends or business associates of management in 11% and 18% of the investments respectively. Only 6% of them found the entrepreneur through one of the matchmaking services. Most important, from the entrepreneurs' point of view, these investors generally did not want a control position: only 10% had a controlling interest and almost half (46%) took less than 25% of the equity. This reflects the common observation that informal investors believe in their entrepreneurs, while the formal investors are concerned about them.

The informal investors are highly active, despite this being a part-time occupation for them. In the three years prior to the survey, the 73 people in this sample made 151 investments, totalling more than $31 million. In the year before the survey, they had reviewed 1,174 deals (17.5 per

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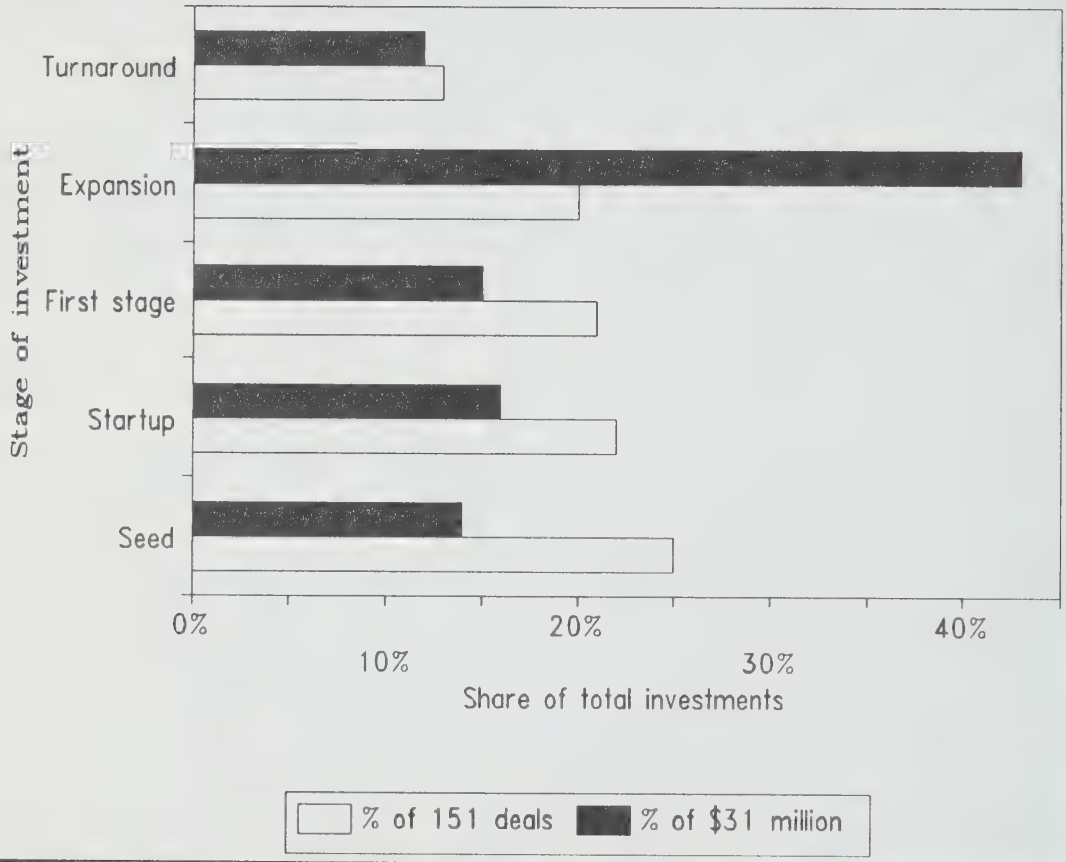
[2]Source: Ibid. *Financing Early-Stage Companies*

person), seriously looked at 219 and invested in 74. As Chart 6.5 shows, these investments were heavily concentrated in early-stage investments.

Chart 6.5
Informal investors put their money in early-stage financings

Distribution of the number and amount of financings by informal investors, by the stage of the business being financed

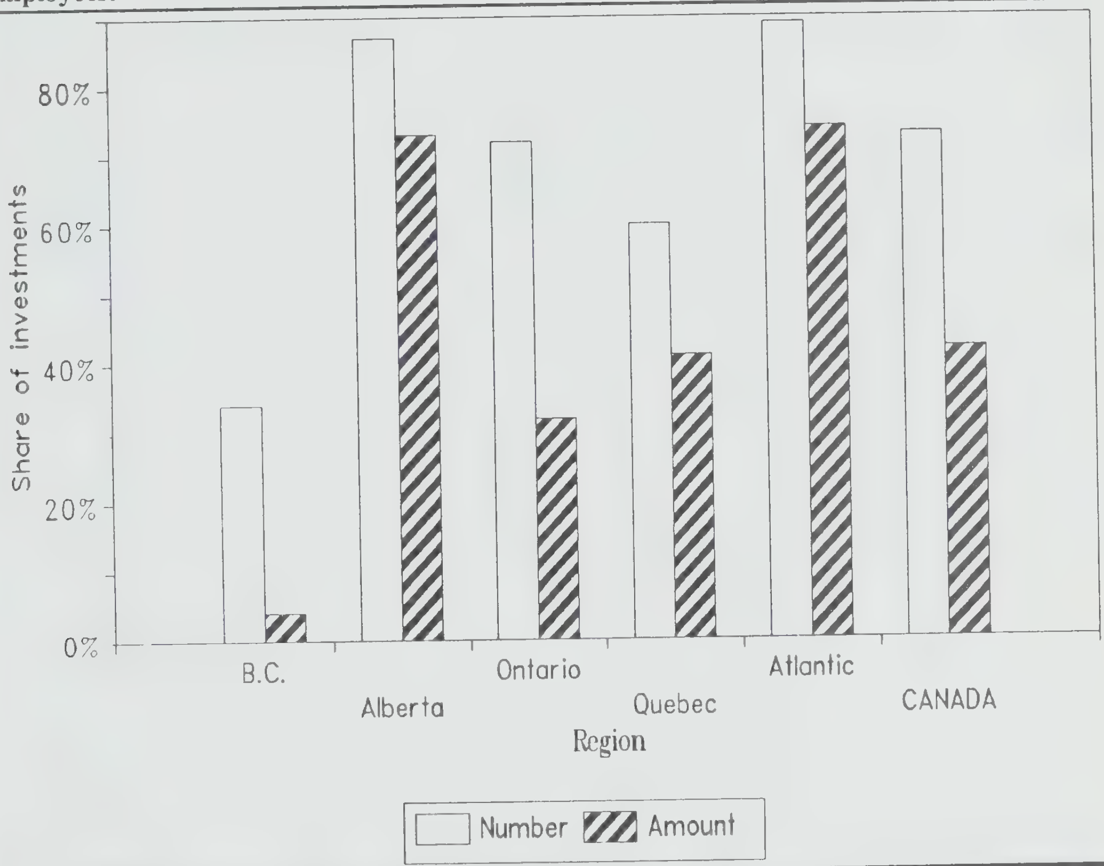


Early-stage investments are generally smaller than expansion financing. In this sample, the average investment in early-stage financings was $137,000, compared to $444,000 for expansions and $190,000 for turnarounds. As Chart 6.5 shows, the three early-stage categories of seed, startup and first-stage financings accounted for 68% of the number of investments and 45% of the amount invested, significantly higher than the formal investors. As a result, the average size of the investment was slightly more than $200,000 for the informal investors, compared to $1.1 million for all deals in the formal venture capital industry in the private

sector (and $620,000 in early-stage deals in 1988, $800,000 in 1989). Most of their investments were in very small firms - almost three-quarters were in firms with fewer than 10 employees, as Chart 6.6 shows.

Chart 6.6
Where the smallest firms are popular

Share of informal investments, by number and amount, going to firms with fewer than 10 employees.



Not only are these investors prepared to put their money into early-stage companies, they also appear to have realistic expectations as to when they can sell their investments. Only 11% of them expected to liquidate their investments within three years; 35% expected to hold for three to five years and another 35% for five to 10 years. Almost a fifth said they expected to be in for more than 10 years or the holding period was "not important" for them. Their expectations for the money they would earn on their investments were reasonable, though still higher than those of their counterparts

in the U.S. A quarter expected returns on investment of less than 20%, 45% expected to earn 20% to 30% and 15% are waiting for earnings of more than 30%. Fully 14% said they did not even think about rates of return.

Informal investors tend to invest close to home, partly because that's where they are more likely to know the management of their investments, and partly because that enables them to be more directly involved in the venture. Only 15% were not actively involved in some way, as Table 6.2 shows:

Table 6.2
Informal investors like to get involved

Participation in company affairs by informal investors		
Extent of involvement	**Canada**	**U.S.**
None, other than reviewing periodic reports and attending shareholder meetings	15%	17%
On the board of directors	31%	15%
Provide consulting help, as needed	28%	27%
Work part-time with the firm	12%	22%
Work full-time with the firm	13%	17%
Other/unknown	1%	2%

They also tended to invest with co-investors in syndicated situations, as Table 6.3 shows. Fully one fifth invested with five or more co-investors. Informal investors in the U.S. are even more inclined to syndicate their investments than their Canadian counterparts. More than 70% of the Americans had two or more co-investors, compared to 48% in Canada. Only 9% of the Americans invest entirely on their own, compared to 38% of the Canadians. The degree of linkage with the formal venture market in Canada is probably overstated, because this sample of investors was drawn from lists compiled, in part, with the help of venture capitalists.

Table 6.3
Informal investors like to syndicate their deals

Comparison of Canada and U.S. informal investors in terms of their links with other informal investors and with formal venture capitalists

Number of informal co-investors	**Canada**		**U.S.**	
	#	%	#	%
0	58	38%	34	9%
1	21	14%	82	21%
2 to 5	41	27%	173	44%
More than 5	31	21%	102	26%
Total	**151**	**100%**	**391**	**100%**
Co-investment with formal venture-capital investors				
Yes	26	17%	40	4%
No	125	83%	924	96%
Total	**151**	**100%**	**964**	**100%**

Unlike the formal venture capital market, these people do not have any strong preferences for how they liquidate their investments. Half of them anticipated selling their shares back to the company or to another company; another fifth expected to sell to another insider; only 10% anticipated a public offering on the stock exchange.

How Canada's fast-growing ventures stack up to their U.S. counterparts

Canadian and U.S. venture capitalists invest roughly the same proportion of their funds in early-stage financings - about 25% - but that's where the similarity ends. A recent study[3] compared 42 Canadian firms that had been financed by venture capitalists in the early stages of growth with 38 comparable American firms. Eight venture capital firms were involved in each case and the sample was selected from their portfolios to ensure that the investors were familiar with their investments. The major conclusions to emerge from the comparison are:

[3]Source: Ibid. *Financing Early Stage Companies*

- Only 17% of the deals and 4% of the accompanying dollars went to seed companies in Canada, compared to 45% of the deals and 28% of the dollars in the U.S. While a significant proportion of the U.S. venture capitalists who invest in early-stage companies do so at the seed stage, most Canadian venture capitalists will not invest until the firm has reached the startup stage.
- Canadian venture capitalists wait longer than Americans before they will invest. The average age of early-stage businesses in which Canadians invested was 2.7 years, compared to 1.3 in the U.S.
- The firms which Canadian venture capitalists chose were also bigger than those chosen by their American counterparts. The average number of employees in Canadian early-stage companies was 14.8, compared to 6.4 in the U.S.
- Technology firms accounted for 45% of the investments and 51% of the dollars in Canada, compared to 84% and 88% respectively in the U.S. sample. Moreover, the Canadian investments are concentrated in computer-related firms, which have lost the potential for really significant gains as the industry has become more established in the past decade. The leading-edge technologies now are the medical and health related sectors, in which 42% of the U.S. capital was invested, compared to 4% of the Canadian capital.
- Canadian investors take less equity for their investment than Americans do. In the U.S. sample, 68% of the startup-stage companies had sold more than half their equity to venture capitalists, compared to 39% of the Canadian companies. Almost two-thirds of the seed-stage companies in the U.S. were controlled by venture capitalists, compared to 16% in Canada.

Part of the reason for the lower shareholdings of the venture capitalists in Canada is the unwillingness of Canadian entrepreneurs to relinquish control positions; they tend to sacrifice growth potential if it conflicts with the preservation of their equity position. To this must be added the much higher valuation that American investors place on early-stage companies. In all early-stage companies, the U.S. venture capitalists valued the companies before the financing at an average of $3.3 million, compared to $1.6 million in Canada. This means that not only do the American investors take a bigger share of equity, but they also pay more for each percentage point of equity. The result is much better funded firms, equipped to grow with backers who stand prepared to provide follow-up financing.

The major difficulty for Canadian venture capitalists is that they simply do not have as much confidence in the management capabilities of Canadian entrepreneurs - and quality of the management is the single most important factor in the investment decision. One indication of this comes from the answers the venture capitalists provided when they were asked to estimate the average amount by which they discount entrepreneurs' sales and profit projections. For the first year's projections, Canadians discounted sales by 48% and profits by 75%, while the Americans discounted sales by 8% and profits by 17%. For three-year projections, the Americans discounted projections more heavily (40% and 50% for sales and profits, compared to 29% and 28% by the Canadians), but this is probably a reflection of more conservative projections in the medium term by Canadians than Americans.

One measure of management expertise is experience in the industry and the management teams of early-stage companies in the U.S. had been in their industry for significantly longer than their Canadian counterparts. The President had an average of 11.1 years' experience in the industry, compared to 6.7 for Canadians. Similar disparities exist for the other key positions: for Vice Presidents of Sales and Marketing, 9.9 years compared to 6.0 years for Canadians; for Vice Presidents of Research & Development, 12.8 in the U.S. and 5.6 in Canada; for Vice President of Finance, 2.5 in the U.S. and 0.8 in Canada; and for Vice President of Manufacturing, 10.2 in the U.S. and 7.2 in Canada.

North America's fastest growing companies

In a comparison of the 50 fastest growing public companies in the U.S. and Canada[4], the Canadian companies, once again, lag far behind in growth. Between 1984 and 1988, the U.S firms increased their sales revenues by 204% on average, compared to 84% in Canada. Between them, the 50 U.S. companies had sales of $6.5 billion, compared to $2.4 billion in the Canadian companies (not a bad performance, all the same). As Chart 6.7 shows, 82% of the Canadian firms grew at less than 100% a year, while all of the U.S firms grew at more than 100% a year; 20% of the U.S. firms grew at more than 300% a year, while none of the Canadian companies did so.

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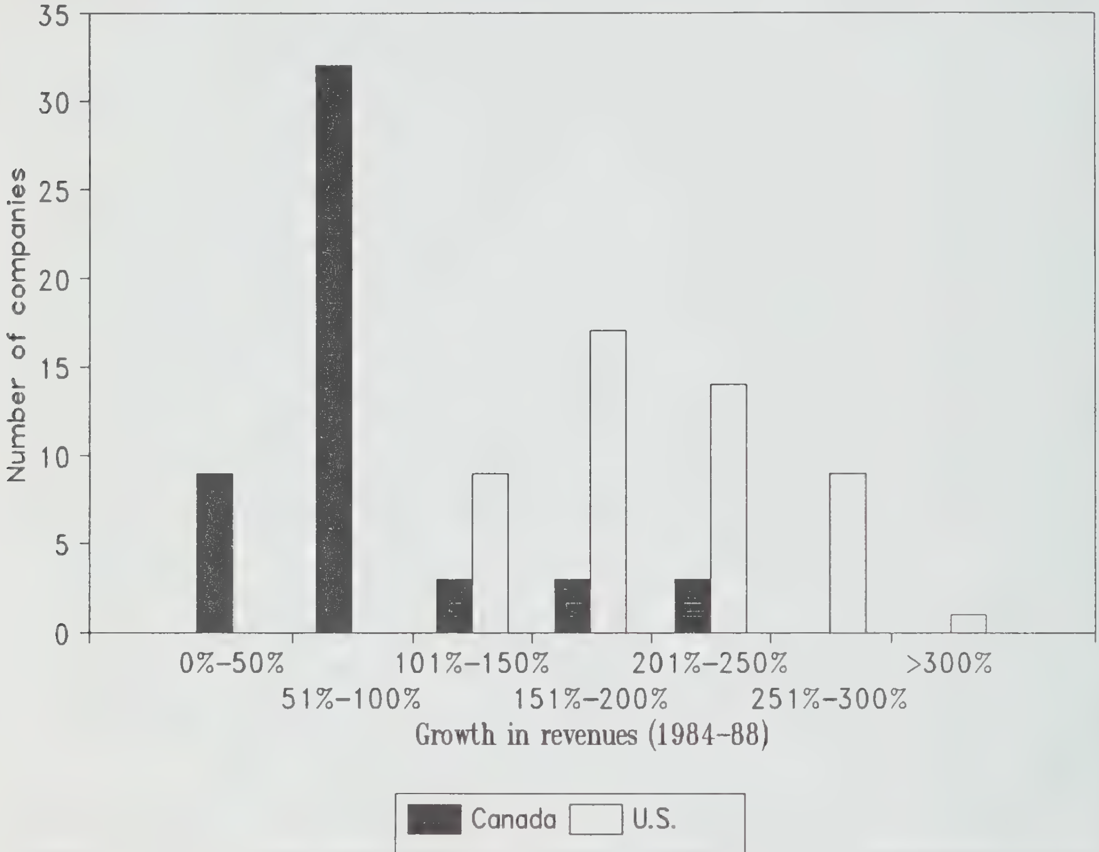
[4]Source: *INC Magazine* and *Canadian Business Magazine*

Chart 6.7
The fastest growing firms grow much faster in the U.S.

Distribution of the 50 fastest growing companies in Canada and the U.S. by average annual rate of growth, 1984-88



Some other findings in the comparison:

- 58% of the fastest growing firms in Canada were in Quebec; 13% were in Ontario, far below its share of the economy.
- Half the American firms were technology-based, compared to 29% in Canada.
- The combined revenues of the Canadian firms in 1988 were 37% of their counterparts in the U.S. In 1984, the combined sales of the Canadian companies were four times as big as those of the U.S. companies. In other words, the U.S. firms collectively increased their sales 91 times during the period, compared to eight times by the Canadian firms.

- About 80% of the firms in both the lists went public during 1984-88, but the Americans raised $15.6 million each on average, while the Canadians raised $5.9 million. This gave the U.S. firms a more solid basis on which to grow: their average debt/equity ratio was 0.87, compared to the Canadians' 1.46. This helped them, in turn, increase sales faster: their ratio of sales to employees was $172,000, compared to $107,000 in Canada; and their ratio of sales to equity was 2.83, compared to 1.56 in Canada.
- Consistent with much of the research in this chapter, the Canadian companies were also quite a bit older than the U.S. firms. In 1984, 86% of the U.S. firms had been founded in the previous five years, while only 30% of the Canadian firms had been.

As one final indication of the gap in the Canadian market for financing early-stage companies, 26 of the 50 firms in the U.S. had venture-capital backing, compared to only six in Canada. Of the U.S. firms, 22 had raised venture capital when they were still private and 20 were still in the early stages of development when they obtained this financing. On average, these 20 firms received about US$17 million in venture capital, through three separate rounds of financing that involved 11 different funds. The six Canadian firms did not fare as well. On average, the venture capitalists invested about $3 million in each of these firms. Five received only one round of financing from one fund and were at the expansion stage when they received the venture capital. Only one company received financing when it was at an early stage of development, although it was past the startup stage.

Part III

The Role of Government

An outline of the strategy of Small Business Ontario, which is the branch of the Ministry of Industry, Trade & Technology that focuses the government's role in small business. Programs delivered by other government agencies are also reviewed, with particular attention to the introduction of entrepreneurship courses in Ontario's high schools.

CHAPTER 7
SMALL BUSINESS ONTARIO

Within the government of Ontario, responsibility for policies and programs relating to small business rests primarily with Small Business Ontario, which is the new name of what used to be the Small Business Branch of the Ministry of Industry, Trade & Technology. The new name reflects a new mandate, which seeks innovative responses to policy and program issues in a changing environment.

In 1985, the Small Business Branch developed a mission for itself to promote the interests of entrepreneurship and of entrepreneurs in the context of:

- A province largely unaware of the contributions made by entrepreneurs to the general well-being of all its economic players;

- A rapidly growing client base of entrepreneurs who were often ill-prepared for the rigours of running a small firm; and

- A stable political and economic environment.

The first of these assumptions may still be true to a degree, but the other two have changed in the intervening five years. Entrepreneurs who are in business today have survived some rough passages, developing, in the process, skills that would have been out of the reach of their predecessors of 10 years ago. This is partly a result of the enormous sophistication that personal computers have brought to even the smallest of businesses, partly a reflection of global markets so competitive that well-honed business skills (as opposed to technical skills) have become a core necessity rather than a luxury. Another element in the evolution of the client base of small businesses and entrepreneurs is that the ethnic make-up of the province is beginning to make itself felt in the field of entrepreneurship, and the growing body of new-Canadian entrepreneurs is changing the mix of needs to which the established institutions of this province must respond. Finally, the political and economic environment has become significantly more volatile in the past few years. Governments do not have much room to manoeuvre any more and voters are sending politicians mixed messages,

making it more difficult to establish stable political frameworks for provincial and federal economies.

In its new plan, designed for 1990-95, Small Business Ontario (SBO) has developed a more ambitious vision for the contribution it can make to the province's entrepreneurs, current and future. The goals comprising this vision include:

- An Ontario sympathetic to the entrepreneurial ethic, valuing innovation, self-reliance and calculated risk-taking.

- A growing number of Ontario entrepreneurs owning and operating their own businesses or applying their talents within larger organizations.

- Greater numbers of small businesses entering export markets.

- An education system that fosters the entrepreneurial ethic among our young people.

- A province-wide information network providing relevant bottom-line intelligence to both startup and established entrepreneurs.

- An active private sector involved and committed to supporting the growth of entrepreneurship through independent or joint public-private initiatives.

- Government at all levels sympathetic and responsive to the need to maintain a public policy environment conducive to entrepreneurship.

- A widely recognized Small Business Ontario generating interest and support in both the private and public sectors.

This vision will be implemented by focusing on three areas: education, business services and advocacy. The first will seek to prepare potential entrepreneurs for the rigours of their career, as well as enhance the public's perception of the value of entrepreneurship to their general well-being. The second will attempt to meet the growing needs of new and existing entrepreneurs. The third will improve the business climate for entrepreneurship within both the government and the province in general. The goals in these three areas can be pursued effectively because the branch

has already developed a well-established organization with an international reputation for effective programming and for its network of regional operations.

The short-term goals toward these long-term objectives include an extensive list of activities planned for 1990-91 (some of which have been implemented already), including:

- Establish 13 new Self-Help Offices (see later this chapter for more on Self-Help Offices);
- Improve access to the Self-Help Offices and services for local businesses;
- Integrate into SBO's activities with the youth startup programs transferred to it from the Ministry of Skills Development;
- Expand entrepreneurship education; and
- Achieve some relief for small firms from ever-rising levels of taxation.

Almost half of SBO's staff are delivering assistance to startups through the Self-Help Offices scattered across the province. Another fifth of the staff are working on the range of youth programs administered by SBO. The balance concentrate on advocacy, representing the interests of small business in the government, administering the Technical Personnel Program (see Chapter 9) and furthering entrepreneurship education. Together these departments handle 150,000 inquiries a year, register 15,000 new clients, distribute 115,000 self-help books to entrepreneurs, finance about 1,000 businesses a year and sponsor 185 seminars, attended by some 9,000 participants.

For the balance of the five-year plan, from 1991 to 1995, SBO has mapped out four strategic directions for itself:

1. *Supporting youth entrepreneurship.* This entails working with the Ministries of Education and Colleges & Universities to introduce entrepreneurship education at all levels of the system. It will include Visions, a program that helps local school boards and the teaching community to find role models who can come into their classrooms to assistthem in teaching the importance of entrepreneurship in our society. In

addition, SBO administers Youth Start-up Capital, a program that lends students and recent graduates funds to start new businesses, either permanently or for the summers (more on this later in this chapter).

2. *Enhancing business services and making them easily accessible*. The bulk of these services will be delivered through the Self-Help Offices, which are locally co-sponsored throughout the province. The activities include direct referral assistance, learning materials and a province-wide network of data and information useful to small businesses. SBO has also developed programs to support the adoption of technology and to upgrade the competitiveness of existing businesses that need to improve their management and international marketing skills. Beyond these generic goals, SBO intends to identify and serve unique groups that require special advisory or financial services.

3. *Improving the climate for entrepreneurship and small business in Ontario*. SBO will work within the government to promote a healthy environment for business startups and growth, enhancing other ministries' sensitivity to entrepreneurship. An important part of this effort is the acquisition, through research, of more data relating to entrepreneurship and the nature of its role in the province. A major focus is the provision of innovative financing options to supplement the private-sector marketplace.

4. *Upgrading the delivery of Small Business Ontario's programs and service to provide leading-edge product support and customer service*. This entails a number of initiatives, including:

- Employing new technologies in product development and support;
- Developing administrative techniques to manage decentralized, co-sponsored operations;
- Increasing promotion and communication activities to ensure awareness of SBO services;

- Acquiring central agency approval for directly accepting revenue as a cost offset;

- Expanding private-sector co-sponsorship of services and enhancing activities to generate revenues;

- Developing a system of continuous program review to ensure the most efficient allocation of funds;

- Enhancing staff development and employment equity initiatives; and

- Seeking to improve staff incentives, standards and feedback mechanisms for customer service.

Self-Help Offices

By the end of 1990, Small Business Ontario had 26 Self-Help Offices established around the province. The first two were opened in 1985, and as the concept proved itself, the network expanded rapidly before reaching its current level: six were added in 1987, eight in 1988-89 and the final 11 in 1990. Most of them (22) are run jointly with the municipality in whose offices they are located. There are also about 100 kiosks in smaller communities too small to support a full Self-Help Office. The kiosks are usually located in the city hall and provide instructions on how to get to the nearest Self-Help Office and how to obtain basic material for starting a business.

The fundamental premise of the Self-Help Offices is that they do not provide direct assistance to small firms using their own resources; rather, they aim to refer their clients to the right sources for information or advice. Each office has a consultant and a good selection of relevant literature. The consultants are equipped to guide new entrepreneurs through the preparation of a business plan and will even review the results, but they will not prepare them for the clients.

Apart from the one-stop referral service to incipient entrepreneurs or entrepreneurs experiencing some difficulty, the Self-Help Offices have two other major areas of endeavour:

- Seminar programming. This is currently being performed by staff in Small Business Ontario who give 185 seminars a year, covering the

topics of starting a new business, marketing, advertising and franchising. It is expected that ultimately, the Self-Help Offices will run all these seminars, using local experts.

- Building a network. This is intended to provide the people who service small businesses with a network of personal contacts through which they can improve their understanding of their market. It is expected the network will incorporate the local chambers of commerce, government people who deliver programs for small business, bankers, lawyers and accountants.

Financing

The marketplace for matching entrepreneurs with investors has never been an easy one. There are countless anecdotes lamenting how each of the two parties has been burned by the other. In many cases, this boils down to a problem of perception - each party values its contribution to the mix more highly than the other. In other cases, there are real difficulties because of insufficient expertise on both sides of the negotiating table. There can be no definitive solution to such a human problem. The marketplace for investing in entrepreneurial ventures must always be difficult, simply because the entrepreneurs' plans are so ambitious, the potential gains and losses so large, that allocating rights and benefits is problematic, at best. The only entrepreneurs who express their satisfaction with investors are those who can live without additional funding, because they can just as easily cancel or postpone their plans as go ahead with them. The much bigger number who complain that investors are too conservative or too greedy are entrepreneurs who want very badly to proceed with their plans, but cannot do so unless they find an investor. For them, "fair" deals are hard to come by.

Whatever perceptions and feelings they may have of investors, entrepreneurs devote a lot of their time and energy to raising capital for their ventures, old and new. It has been found[1] that entrepreneurs spend up to 40% of their time raising money in amounts of $50,000 to $500,000. The 1988 report of the Premier's Council found that lack of equity capital was identified as a constraint to growth by 74% of the firms its researchers interviewed. Numerous other studies have found that Canadian small

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[1]Source: Allan Riding, Associate Dean, Faculty of Social Science, Carleton University

businesses are chronically undercapitalized and excessively reliant on debt as opposed to equity capital, rendering them vulnerable to high interest rates and economic downturns.

The financial markets that exist to fund these entrepreneurs is, in general, well developed. At the grass-roots level, there is a large, dispersed and anonymous body of wealthy individuals who invest in startups and high-risk ventures of entrepreneurs whom they know personally. Much of this is the so-called "love money" of relatives and friends, but there is also an important and large number of professional investors operating on their own in high-risk situations. Attempts are being made to facilitate the connection of these individuals with promising ventures in the fields in which they would like to invest. An example of this is COIN (Canada Opportunities Investment Network), a computerized databank designed to link investors with entrepreneurs, sponsored by the provincial Chambers of Commerce with the support of the federal and provincial governments, Xerox and Price Waterhouse. The major difficulty with these networks is that they depend on personal contact and referral, so are not necessarily susceptible to organization. Budding entrepreneurs who don't have the personal contacts still find it extremely difficult to raise startup capital.

Beyond the informal investor networks, the formal, private-sector venture capital industry has generally abandoned startup financing (see Chapter 6). For them, it is too time-consuming to be profitable, so they are looking at bigger deals (more than $1 million) in more established companies that are in a growth spurt. This is a very narrow market, however, and leaves a significant market gap in the financing of growth-oriented smaller companies that have outgrown the informal investor network. These companies often rely too heavily on banks, putting themselves in dangerously over-leveraged positions.

Within this imperfect marketplace, there is scope for governments to alleviate some of the suffering. This involves, on the one hand, improving the entrepreneurs' understanding of and presentation to investors and, on the other hand, improving the investors' odds, both through offering better yields and through encouraging the development of better qualified people on both sides of the table. By bringing both parties closer to a deal at the outset, governments can act as catalysts to minimize the ample opportunities for misunderstanding. Governments all over the world have experimented with numerous techniques for doing just this, trying everything from direct

investment themselves to piggybacking private investors, to matchmaking. Many of the techniques have found useful applications, but there have been too many missteps along the way, involving embarrassing losses of government funds. Small Business Ontario does not administer directly any of the government-sponsored financing programs in the province, (apart from Youth Startup Capital), but it does monitor their effectiveness, promote their availability, and recommend changes. The financing programs available in Ontario include, among others:

- *New Ventures*. Designed for entrepreneurs who do not have the necessary collateral for commercial loans, this program guarantees loans at prime rate plus one percent for qualifying businesses. The entrepreneur's own equity investment must be an amount at least as much as the loan (except in Northern and Eastern Ontario, where the equity requirement is 50% of the loan) and must undertake to hire one person within the five-year term of the loan. Approval is contingent upon the completion of an acceptable business plan. The program has been extremely successful. Since inception of the program in September of 1986, 16,695 loans have been approved, 29% of which were in Northern and eastern Ontario and 34% of which were to women. At the end of the third year, only 20% of the loans were in default - a figure so far below the average for all firms that it is almost certain to rise.

- *Ontario Development Corp. (ODC)*. Along with the Northern ODC and Eastern ODC, the corporation makes loans and loan guarantees to secondary industries, exporters and tourist operators. The ODC helped more than 1,300 businesses in 1989-90, 600 of them manufacturing firms. Qualified firms can receive loans up to $500,000 and loan guarantees up to $1 million. Tourist operations funded under the Tourist Redevelopment Incentive Program (TRIP) can obtain loan guarantees up to $1 million if they are new operations, $750,000 if they are recreational developments. To qualify, a business must provide significant benefit to the region in terms of jobs, introduction of new technology or industrial diversification.

- *Canada Opportunities Investment Network (COIN)*. (See earlier this chapter).

- *The Federal Business Development Bank*. Owned by the federal government, FBDB provides financial assistance in the form of loans, loan guarantees and equity investments; it also assists small businesses through financial planning and management services (including Counselling Assistance to Small Enterprises and a wide range of conferences and seminars).

- *Innovation Ontario Corporation*. A crown corporation associated with the Ministry of Industry, Trade & Technology, Innovation Ontario provides equity and quasi-equity capital to technology-based firms in the early stages of development. The investment may be in the form of shares or a royalty agreement, but not grants or loans. Innovation Ontario prefers companies that are beyond the research stage, have assembled the beginnings of a management team and appear to have the potential for growth.

  To be eligible a business must have a product or service that is technically and commercially viable. It must also be able to demonstrate the competence and commitment of its management team and have realistic financial projections. Normally, the corporation would expect to sell its interest to private-sector interests within three to five years.

  In its first four and a half years, the corporation has assessed 1,234 of the 1,346 detailed business proposals it has received. It has invested $26 million in 156 companies that are developing a wide range of commercially viable technologies. These include software packages, electronic animal identification, automated retailing systems for liquid products, design components for printed circuit boards, biotechnology and computer-based security systems, to name just a few. In 1988, the corporation backed more than half of the Ontario companies that secured venture capital financing in the computer, medical and industrial automation sectors.

- *Youth Startup Capital.*

  This program was transferred from the Ministry of Skills Development to Small Business Ontario in April, 1990. Its mandate consists of three objectives:

  to develop and encourage entrepreneurial activity among young people in Ontario by promoting entrepreneurship and small-business ownership as a viable career option;

  to provide access to business financing not normally available to young people because they lack experience, stability or collateral security or because they are too young; and

  to assist in the development of entrepreneurial skills, education and an understanding of business ownership, thereby preventing some major causes of small-business failure.

Youth Startup Capital has two divisions:

☐ *Student Venture* provides interest-free loans of up to $3,000 from April 1st to September 30th. To qualify, students must be 15 or over, returning to school full-time in the fall and must operate their businesses during the summer period.

☐ *Youth Venture* guarantees loans of up to $7,500 for five years to young people aged 18 to 24 who have completed their schooling. The age limit is extended to 29 for, youths who graduated or left full-time study at a post-secondary institution or obtained a trade certificate within the previous 12 months. The business must be less than six months old and the youth must have invested equity capital equal to 20% of the loan amount; it must also be operated on a year-round basis. Interest on the loan is paid by the government for the first year. From the 13th month on, the youth must pay interest plus 2% of the principal every month.

Both these programs are co-sponsored by the Royal Bank, the Ontario Chamber of Commerce and local chambers of commerce and Boards of Trade. La Fédération des Caisses Populaires also co-sponsors Youth Venture.

Both programs have been highly successful. Table 7.1 shows the volume of lending in the two programs since 1987-88. Student Venture Capital has financed about 9,000 businesses since it was started in 1973 and Youth Venture has financed more than 5,000 since 1984 when it was started. In 1989-90, these loans created 2.5 jobs each and generated sales of $23 million and $60 million respectively.

The volume of loans has fallen slightly since 1988-89, probably due to tightening economic conditions. The average age of the participants was younger, indicating that older students and youths were shying away from starting their own businesses and younger ones were turning to this option more often. It is reasonable to suppose that the younger students had no other choice because of the difficulty they had finding summer jobs and the more mature students who were less inclined to start a venture because of the more risky economic climate.

In 1990, about 85% of the participants in Student Venture were male and almost two-thirds were in university. For the Youth Venture program, 28% of the participants were females and almost 70% had obtained post-secondary education. More than half the participants in both programs were aged 20-24.

The default rate has been low - 82% repay their Youth Venture loans and 85% repay their Student Venture loans. If Student Venture loans are not repaid at the end of September, or Youth Venture loans are not repaid as agreed, the participants become liable for interest charges. If this is not paid, their credit rating, their eligibility for Ontario Student Assistance Program and their eligibility for future Venture Capital loans may all be affected.

Table 7.1
Startup financing for young people

Details of applications made and approved for Student Venture and Youth Venture loans in the Youth Start-up Capital program

Program	**1990-91**	**1989-90**	**1988-89**	**1987-88**
Student Venture				
Applications received	935	1,058	1,321	1,265
Loans approved	865	943	1,196	1,101
Participants	984	1,132	1,412	1,294
Principal advanced	$2.5 million	$2.7 million	$3.4 million	$3.0 million
Youth Venture (to October 31, 1990)				
Applications received	581	1,294	1,495	1,277
Loans approved	486	915	968	803
Participants	536	1,033	1,093	883
Principal advanced	$3.4 million	$6.4 million	$6.7 million	$4.5 million

Youth Start-Up Capital also provides support to the participants, by encouraging linkage with the program co-sponsors, directing participants to local seminars and providing referrals to organizations funded federally, provincially and locally for assistance.

Customer service

Ontario businesses of all sizes must deal with an array of provincial regulatory and licensing legislation administered by some 20 separate ministries and agencies. Employers must identify legislation and regulations that apply to their businesses; ascertain procedures for meeting obligations from three to nine ministries; and respond on an individual basis to each ministry or agency with a variety of forms and information. To all this must be added the even more complex requirements of dealing with the federal and municipal governments. This regulatory environment is a major irritant in the government's relationship with the business community, and one of the most promising ways to tackle it is to move toward some form of one-stop service, that can route the governments' requirements for each business through one channel.

This is easier said than done, but Small Business Ontario has moved in that direction by establishing the Self-Help Offices and a toll-free hotline. Technology may offer further solutions that could revolutionize this

relationship. Computer networks, locally accessible databases and facsimile machines may allow the handling of federal and provincial requirements by remote control, but this would require significant co-operation of many differing jurisdictions. It is a challenge that is being addressed.

Other issues

There are a number of other issues that Small Business Ontario watches closely:

- An effort to develop suppliers has been mounted for some time in the Ministry of Industry, Trade & Technology. The industrial development review process is administered by the supplier development section, which monitors government purchases for more than $250,000 (or with a significant high-technology content), with a view to encouraging Canadian sources of supply. The section's comments may be used in the tendering or bid evaluation process to improve industrial development in Ontario. In addition, this section stages a biannual "reverse" trade show, called Source Ontario, which displays the purchases of large Original Equipment Manufacturers. Thousands of small firms attend, seeking opportunities to generate new clients.

- Payroll taxes[2] in 1991 are largely unchanged from 1990. The premium for the Employee Health Tax has not changed in 1991. Premium rates for Unemployment Insurance are also unchanged, although the maximum payable by employers has been raised to $1,113.84 in 1991 from $1,048.32 in 1990. Premiums for the Canada Pension Plan rose to 2.3% in 1991 from 2.2% in 1990 and the maximum employer contribution rose to $632.50 in 1991 from $574.20 in 1990. Workers' Compensation Board rates were reclassified but the average did not change greatly.

- The pay-equity legislation advanced another step on January 1, 1991, when firms employing more than 100 people were required to post their plans for attaining equal pay for work of equal value. Firms employing 50 to 100 must develop a plan, although they don't have to post it.

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[2]See *State of Small Business, 1989* for a full commentary on payroll taxes.

- The 1990 budget granted significant concessions to small firms in connection with the collection of the Retail Sales Tax. The amount that retailers are allowed to hold back from the tax they collect as payment for the expense of collecting the tax was raised to 5% with a cap of $1,500 from 4% with a cap of $1,000. To further aid small firms, the government also permitted an immediate deduction for corporate Capital Cost Allowance purposes of the cost of buying cash registers and other electronic point-of-sale equipment.

CHAPTER 8
TEACHING ENTREPRENEURSHIP

In the spring of 1990, the Ministry of Education introduced its Entrepreneurship Studies program for students in grades 11 and 12. It is an optional program, offering two credit courses at each of three levels of difficulty, and is designed to nurture a spirit of innovation in students. This represents a breakthrough for the promotion of entrepreneurial values in the province, because it will enable students to assess their interest in and aptitude for entrepreneurial activities. However, it also carries some risks. An important objective of the course - changing the behaviour and attitudes of students - may be too big and important a task to be undertaken by one optional course alone. In the mean time, the arrival of Entrepreneurship Studies in school curricula has raised the profile of the subject significantly among both teachers and students. As the course content evolves with experience, it has the potential to add an important dimension to the education system, benefitting both the students and the long-run interests of the economy.

In 1989-90, when the Entrepreneurship Studies course was being tested, the major problems identified were finding qualified teachers and appropriate supporting materials. The response to the market vacuum has been, perhaps, entrepreneurial. Within a year, a large number of institutions had started a wide range of initiatives to support the introduction of the concepts associated with entrepreneurship into the school system. These include newsletters for teachers, competitions for business plans by students, videos, teacher training programs, conferences, surveys of student activities and text books.

This process is being further encouraged by the Youth Entrepreneurship Fund, administered by Small Business Ontario. This fund will dispense $100,000 in the year to March, 1991, on innovative, locally sponsored initiatives which enhance youth awareness and exposure to entrepreneurship. These include conferences, supper networking and student entrepreneur clubs, among others.

Small Business Ontario is not directly involved in setting the curriculum for Entrepreneurship Studies, although it has played a consultative role. It is, however, involved in evaluating the reactions of students who have taken

the Entrepreneurship Studies course. This is done on the first and last days of the course through self-rating questionnaires filled out by the students. Small Business Office also fills a supportive role for the Ministry of Education through its Visions program.

Visions

Visions is a program designed by Small Business Ontario to complement the Entrepreneurship Studies course for students in grades 11 and 12. It is aimed at students in grades 7 and 8, and aims to introduce them to the concept of entrepreneurship, to enable them to recognize the benefits that entrepreneurship can bring to our society and to encourage them to consider entrepreneurship as a viable career possibility. The program was successful when it was tested between February and June, 1990, in 20 schools in four school boards in East York, Toronto and Thunder Bay, so it was extended to another nine schools in September, 1990 and a further eight in January, 1991. It is anticipated the program will be available to all schools in the province in 1992.

The program sent to the 20 schools included material for three lessons, revolving around a visit by an entrepreneur. A supplementary course of an additional seven lessons was prepared by Small Business Ontario and offered on an optional basis. Eight of the schools requested the package, which is strongly activity-based. The teachers thought the program was good, with all but one of the 20 saying they would use Visions again.

The program was taken by more than 800 students, who reacted favourably to it. Almost half of them (47%) said they had a very high or a high interest in entrepreneurship at the end of the third lesson. In an earlier survey[1], only 43% of students said they were likely or somewhat likely to start their own business. More than half the students who participated in Visions found the entrepreneurs' visits interesting (57%) and another 39% found them very interesting. Only 4% said they were bored.

The students were asked to think of a good entrepreneurial project at the end of the program. The most popular ideas were selling school T-shirts, pencil insurance (to replace lost pencils), washable ink, food sales in the cafeteria and putting on dances. Their biggest concerns about becoming an entrepreneur were fear of failing and lack of self-confidence.

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[1]See *State of Small Business, 1989*, Chapter 11, page 152

Entrepreneurship Studies in grades 11 and 12

The Entrepreneurship Studies program prepared by Ontario's Ministry of Education is designed to nurture a spirit of innovation in students. It is specifically not aimed at teaching students how to start a new business, nor is it intended to be an extension of courses in business administration. Rather it seeks to provide students with opportunities to discover that entrepreneurial activities demand vision, a high degree of initiative and skill and that these activities can be in non-commercial as well as commercial ventures. The aims of the program are to provide students with opportunities to:

- ☐ assess their interest in and aptitude for entrepreneurial activities;
- ☐ recognize that entrepreneurial skills and behaviours can be developed;
- ☐ use the process of self-assessment and goal-setting to set personal goals and achieve them;
- ☐ establish the necessary communication skills to enable them to work successfully with others;
- ☐ identify the challenges and rewards of initiative and achievement when applied to a wide range of commercial and non-commercial entrepreneurial applications;
- ☐ develop entrepreneurial skills and attitudes and apply them to personal, school, business and community-service opportunities;
- ☐ understand the role of entrepreneurship and innovation in our society and assess its effect on the quality and level of economic activity in the country; and
- ☐ examine a wide range of entrepreneurship career options.

The Entrepreneurship Studies course is designed to help students understand what entrepreneurial opportunity is, how it can be recognized, how entrepreneurial ideas are generated, what pitfalls can be expected, how to plan for success, and how and where to find assistance or support.

The learning environment for these studies must necessarily be quite different from that for other courses. There are six principles that the Ministry sees as governing this environment:

1. Equal emphasis should be placed on the contents of the course and on the development of self-awareness and self-confidence. The process of learning is as important as what is being learned.

2. The course should be activity-based, enabling students to experience the fun, the creativity, the risks and gains, the mistakes and the excitement that are often part of entrepreneurial activities. An important part of this is fast, direct and regular feedback.

3. In entrepreneurship, there is often no single right way of doing something. Students should be encouraged to analyze alternatives and seek out better solutions rather than the correct answer. Activities should be designed to encourage creative thinking as opposed to the mere processing of information.

4. Teachers should facilitate the careful assessment of potential risk and help students understand the concept of managing risk.

5. Students should learn to understand the context of innovation - how the community, their field of interest, the predominant "climate" all influence opportunities for entrepreneurial activities. Students should examine the process of change and its importance to personal, business, community, national and international activities. They should also be taught to recognize that change can be gradual and evolutionary as well as sudden and revolutionary.

6. The qualities of creativity, innovation and entrepreneurship should be an integral part of the way the courses are delivered in the classroom. The physical environment should recognize these special needs. Classrooms should provide the communications, feedback and even desk arrangements to facilitate the use of media and role-playing, of individual as well as

group activities. Activities should include out-of-class activities, field trips, guest speakers from the community, and case studies of entrepreneurial success stories and failures.

Early in the Entrepreneurship Studies course, students are given the opportunity to determine their own individual aptitude for entrepreneurial endeavours and to measure their skills in these types of activities. They are required to answer the following questions:

What entrepreneurial attributes do I have?
At what level of expertise?
What skills do I have?
What skills do I still need to develop?
Where and how can I practice these skills?

The skills that Entrepreneurship Studies aims to develop in students include the following:

- ☐ The ability to set goals for themselves
- ☐ Achievement orientation, the necessary adjunct to goal-setting
- ☐ Self-motivation
- ☐ Self-confidence, particularly knowing how to turn failure into a positive learning experience.
- ☐ Perceptiveness, the ability to detect rapidly emerging changes in people or the environment
- ☐ Realism, a necessary component of perceptivity
- ☐ Creativity, the ability to see combinations and patterns of things or events that differ from other people's perceptions
- ☐ Perseverance
- ☐ The ability to take rational risks, by learning to identify and manage the hurdles or pitfalls that are likely to stand in the way of an entrepreneurial venture
- ☐ Flexibility, and knowing when to avoid a risk
- ☐ Self-discipline
- ☐ The ability to maintain good health and high energy
- ☐ Interdependence
- ☐ Leadership skills
- ☐ The ability to work productively in a team

The school system is required to give students grades for their courses, but entrepreneurship, by its very nature, presents a challenge in this area. As a component of the assessment of students' progress, teachers are encouraged to ask students to set their own standards of accomplishment, to evaluate themselves and be evaluated by their peers. The students should monitor their own progress continuously throughout the course and learn to examine their own failures as well as those of others. The teacher must, of course, offer guidance in this self-evaluation, stressing the importance of effective communicating, decision making, planning, leadership, the appreciation of when they need help, marketing, human relations, the management of time and record-keeping skills. Teachers are encouraged to be innovative in their evaluation techniques and may consider using performance appraisal forms, for example, or conferences, surveys of skills and attitudes, projects, interviews and tests or examinations.

The structure of the content of the Entrepreneurship Studies course is arranged at three levels - basic, general and advanced - as is shown in Table 8.1. The structure for general and advanced levels is the same but the content is different.

At the basic level, the curriculum attempts to define the principal terms associated with the leadership and the personal skills required to be an entrepreneur. An entrepreneur is defined as:

> "someone who (a) brings together various resources in order to pursue a venture that addresses some need, want or problem in an innovative way; (b) has the ability to see what others have not seen and the courage and skill to act on the opportunities perceived; (c) is an 'agent of change' who challenges the status quo; and (d) takes controllable risks, which are different from gambles."

The course material stresses that entrepreneurial attributes can be learned or acquired and invites students to list those they feel they possess and those they don't. [Included in the list are skills such as the ability to generate the right idea for a specific opportunity, to prepare and manage an effective plan, to communicate effectively, to make the right decision and to build an effective team.] Students are encouraged to assess their abilities through skill-testing procedures, compare them with those of a successful entrepreneur and develop a plan for improvement in their weak areas. They are particularly instructed on the importance of self-confidence and invited

to visit a day-care centre to see how this attribute is instilled in very young children. They learn what motivates entrepreneurs, especially the thrill of a challenge.

Table 8.1[2]
High school curricula for entrepreneurial studies

Suggested curriculum modules for Entrepreneurship Studies in grades 11 and 12 in Ontario high schools

Unit	Basic Level	General & Advanced Levels
I	Setting goals	What is an entrepreneur?
II	Entrepreneurs & entrepreneurship	Entrepreneurial careers & lifestyles
III	Entrepreneurial attributes	Invention, innovation and entrepreneurship
IV	The spirit of entrepreneurship	The entrepreneurial process & the importance of planning
V	Entrepreneurial skills	Identifying & evaluating opportunities
VI	Identifying & evaluating opportunities	Identifying & evaluating ideas
VII	Identifying and evaluating ideas	Developing an entrepreneurial action plan
VIII	Innovation & meeting the challenge	Implementing a plan and managing resources
IX	Sources & resources	
X	Planning & evaluation	
XI	Management & effective teamwork	

The course distinguishes between opportunities and ideas as follows:

> "*Opportunity* arises from a change or a trend that has resulted in the generation of a problem, need or want...an *idea* is a proposal for a solution to a perceived opportunity and many ideas can be generated in response to an opportunity."

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[2]Source: Ontario Ministry of Education

Students are invited to perceive some opportunities within their communities, generate a number of ideas for the solution or exploitation of the opportunity, and prepare an appropriate marketing plan. The course material defines a venture as:

> "an activity that (a) has a clearly defined goal; (b) is a response to a perceived opportunity; (c) is an idea brought to reality; (d) is the result of the initiative of an adventurous person or group of people; (e) presents a considerable challenge; (f) involves the commitment of a number of resources; and (g) involves a considerable amount of planning."

The students are expected to identify the resources they need to implement the idea they have picked as the best out of their list of possible ideas. Then they must establish the cost and availability of those resources. In making their plans, they should identify potential resistance to the success of their venture and develop appropriate contingency plans.

Finally, in the pursuit of effective management, students in the basic level course are taught the importance of good communication, teamwork, organization, decision-making and record-keeping skills.

At the general level, the course material adds a number of dimensions to the concept of what an entrepreneur is, including:

- ☐ The need for ongoing feedback and the difference between short- and long-term goals;

- ☐ The existence of entrepreneurship in many varied circumstances, including non-commercial ventures, community service and large- or small-scale operations;

- ☐ The recognition that entrepreneurial qualities can be found in both men and women, irrespective of age, education or social background;

- ☐ The existence of factors, which can be imposed by the external environment or can be self-imposed, and which can limit entrepreneurial activity (including information, resources, time, energy and fear of failure); and

☐ The concept of intrapreneurship, which is rewarded by such things as the satisfaction of contributing to the growth, improvement of efficiency of an organization.

Students are taught to assess the changing nature of work and predict future changes through a comparison of working conditions in selected work categories 20 years ago, today and in 20 years' time.

The difference between invention and innovation is spelled out as:

> "*invention* is the creation of a new idea, process, product or service, but not the development or application of it....and *innovation* is the entire process of change that involves the creation, development and application of a new idea, process., product or service in order to satisfy a need or a want or solve a problem."

The concept of risk is expanded at the general level to include the potential loss of money, health, family, security, social life and time. The concept of planning is deepened to the two phases of (a) anticipating the future and (b) determining how to respond to potential future developments that might occur. The students are asked to use case studies to show how probable ineffective planning caused failures in local entrepreneurial activities and outline how better planning might have provided a better opportunity for success. The course material stresses the importance of being able to adhere to a plan while being flexible enough to respond to unforseen developments.

Students are taught to assess opportunities and, having selected a promising opportunity, to experiment with techniques of generating ideas, including brainstorming, constructing scenarios, associating, synthesizing, visualizing and experimenting. The ideas are then assessed, bearing in mind the barriers to ideas, which include inertia, allegiance to the status quo, competition from the ideas of others, lack of interest and failure to perceive a rationale for change.

In the planning process, students are asked to identify specific places in the planning process where it will be necessary to generate alternative courses of action. Finally, they are taught to identify potential problems

when the initiative begins to grow, considering examples of failures from uncontrolled growth. Then they are asked to prepare a list of attributes that have a positive or negative effect on teamwork and explore how they can improve their ability to manage an entrepreneurial venture.

At the advanced level, there is more intellectual structure in the course. In defining entrepreneurs, additional material is added on the barriers to self-confidence and the importance of a need to achieve. In the section on entrepreneurial careers, the students are asked to prepare a cost/benefit analysis of an entrepreneurial career and of other types of employment.

In the section on invention and innovation, they are asked to document the "constant tension between being imaginative and being realistic when generating a creative solution." They are asked to prepare a list of inventions that never became innovations and to recognize that invention and entrepreneurship are necessary for the process of innovation to occur. As illustrations, they are encouraged to identify a number of major changes that have affected all levels of society during the past several decades; also, they are asked to determine the extent to which social reformers were really entrepreneurs and to research the role of entrepreneurs, entrepreneurship and intrapreneurship in the development of Canada.

In the section on planning, the advanced students are introduced to techniques for the preparation of effective plans, including planning guides, flow charts, critical-path analyses and spreadsheets. In the section on the identification of opportunities, they are taught the role of perception in the recognition of opportunities and how different individuals may perceive the same reality in different ways. They are asked to document the importance of curiosity and sensitivity in a variety of successful endeavours. Advanced students are taught the techniques of trend analysis and how to identify the factors that push or redirect a trend. The course material stresses that, "in order to select appropriate opportunities, entrepreneurs must maintain a strategic overview and synthesize any disparate information to make sure that they are always addressing the "right" problem."

Students in the advanced level are taught what is currently known about the thinking process, including the following:

☐ the functions of the left and right sides of the brain;

- ☐ the difference between knowledge and intuition;

- ☐ the differences between logical, linear, deductive and lateral thinking;

- ☐ the search for the *one* right answer versus the generating of various possibilities, including many new, right answers; and

- ☐ the way that learning and maturing affect the creative process in both a positive and a negative manner.

Students in the advanced level are introduced to the advantages and disadvantages of debt and equity financing. They are also taught the difference between managing small and large organizations and asked to summarize a number of different approaches to management, focusing on the management styles that are used to encourage intrapreneurship within a number of exemplary organizations. They are asked to select their own management approach and describe how it would function in a crisis.

Preliminary feedback on the Entrepreneurship Studies program

In May of 1990, Small Business Ontario sponsored a forum that brought together educators and entrepreneurs to discuss the development of the Entrepreneurship Studies course in high schools. It was noted that the schools which have tried the course made progress on one of its major objectives, the achievement of behavioural and attitude changes in students. Changes have been observed by the students themselves, as well as by parents and other teachers. The tangible evidence of this is an improved attendance record. The participants agreed on a number of other issues:

- The curriculum must have a strong bias toward action if it is to succeed. This includes participating in projects and preparing business plans.

- The involvement of the local community adds an important ingredient to entrepreneurship education. Teachers should be encouraged to invite speakers into their classrooms - and not just small business owners, but bankers, lawyers and other members of the community who demonstrate entrepreneurial skills.

- The best teachers for entrepreneurial studies are self-selected, enthusiastic and action-oriented.

- Traditional means of evaluating students may not be appropriate for entrepreneurial studies, because they are learning a process which has few right or wrong answers.

The entrepreneurs who participated in the forum, all of whom had won awards from the Ministry of Industry, Trade & Technology's Youth Start-up Capital program, observed that their immediate families had been a very positive influence in their business experience, particularly because the risk seemed minimal to them thanks to their family's emotional and personal support. They all felt role models or mentors were crucial and that a principal objective of the course should be to build students' self-confidence to reduce the fear of failure. They all agreed, however, that their youth had posed some difficulties in winning credibility.

They furthermore noted that experience is the best way to learn, because the skills needed to run a business are not always acquired in a classroom setting. Of particular interest, it was a matter of a few months between the time they identified their business opportunity and the time they launched their ventures. The research they conducted was, they said, fairly superficial. The most important skills, in their opinion, were understanding cash-flow management and accounting procedures, and the need to be computer-literate.

The Spirit of Adventure

One of the teaching materials released in 1990 was a collection of six videos and an accompanying workbook on "The Spirit of Adventure: Entrepreneurship for Canadians." Produced by the Canadian Foundation for Economic Education, the package's basic approach dovetails with the curriculum prepared by the Ministry of Education, but there are some minor differences in content, as Table 8.2 shows. The videos feature profiles of 35 entrepreneurs who illustrate points made in the lessons. The

videos and accompanying exercises are designed to be presented over 24 to 30 class periods of 45 minutes each.

The project was sponsored by a large number of organizations, including the federal government, seven provinces (Including Ontario's Ministry of Colleges and Universities), the Canadian Bankers' Association and 23 private-sector corporations.

Table 8.2
Content of the video series, "The Spirit of Adventure"

Program #	Program title	Content
1	Catching the Spirit	• Introduction to entrepreneurship • Role & contributions of entrepreneurship • Characteristics of entrepreneurs
2	Developing the skills	• Skills important for effective entrepreneurship • The skills can be learned/developed
3	Recognizing the opportunities	• Defining and assessing entrepreneurial opportunities • Recognizing what gives rise to entrepreneurial opportunities • Ideas are linked to opportunities and need an opportunity to succeed
4	Ideas and innovations	• The nature of entrepreneurial ideas • How to generate and assess entrepreneurial ideas
5	Planning for success	• Potential problems facing entrepreneurs • The importance of planning • Learning from mistakes and failures
6	It's up to you	• Entrepreneurs come from everywhere, in all shapes, sizes, colours and sexes • Entrepreneurship can be applied to any kind of endeavour • Entrepreneurship is a personal decision and, in the end, it's up to you

Junior Achievement of Canada

Of course, long before all these developments, Junior Achievement of Canada was putting its volunteers into schools across Canada giving students the opportunity to experience hands-on the challenge of running a business. This effort has not concentrated exclusively on entrepreneurship,

but it has brought basic business skills to the classroom. The resources brought to the education system by Junior Achievement include a computer model for business planning and a study program of applied economics.

Centres of Entrepreneurship

The Ministry of Colleges & Universities currently funds six pilot centres of entrepreneurship. Their main functions are to develop programs and courses, train teachers, undertake research on entrepreneurship and provide consulting assistance to small business and entrepreneurs. The funding is contingent on the centres raising funding from private-sector sources, although this requirement has been administered flexibly. The six centres are:

North Bay (Canadore College, Nipissing University)
Northwest Ontario (Lakehead University, Confederation College)
Eastern Ontario (St. Lawrence College, Queen's University, Loyalist College)
Centennial College in Toronto
Ryerson Polytechnical Institute in Toronto, and
York University in Toronto.

Small Business Ontario, once again, is not involved in administering these centres, but holds a watching brief for the Ministry of Colleges & Universities.

University Small Business Consulting

This program offers a subsidized consulting service to local businesses, using undergraduate and MBA students as consultants. The consulting services include market research, feasibility studies, accounting, the preparation of business plans and strategic planning, among others. The program is intended to provide local businesses with low-cost help and to provide students with an opportunity to put into practice what they have learned in the classroom. Consultant fees vary from $60 to $250 a day.

In 1989[3], the 16 units averaged fee revenues of $38,400, and grant revenues of $29,100 (the maximum grant that year was $35,000). Most

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[3]Source: *Evaluation of the University Small Business Consulting Program*, prepared by The DPA Group for Small Business Ontario, November, 1989.

units generated about three contracts per consultant but one averaged 10 and two others more than five. Average operating costs were about $66,000 for the four summers in 1986-89, then rose slightly to more than $70,000 in 1990. The average base salary for the consultants was about $7.50 per hour, plus a bonus of about $1,200 at the end of the year. Most students in the program earn $5,000 to $10,000 a summer, although some have been known to earn up to $15,000.

In 1990, the targets set for the program by Small Business Ontario were as follows:

- 375 small firms to be assisted
- 80 managers and consultants to be employed
- $500,000 in cost reductions or revenue increases for the clients
- 255 new jobs to be created.

The program runs from May to August at 16 sites in 15 different universities. In 1990, the Ministry of Industry, Trade & Technology provided each unit with $13,000 at the beginning of the year ($10,000 for the consulting business and $3,000 for the faculty co-ordinator) plus 50% of the fees generated from small-business clients to a maximum total of $25,500. For five universities, the subsidy is extended to 75% of the fees.

The role of the faculty co-ordinator is to recruit the student manager and consultants; review all client proposals and final reports to clients; provide operational and administrative assistance and support to the staff; and receive the Ministry's funding. The student manager's role is to market the program through the media and through the local offices of MITT and the self-help offices; meet with prospective clients; administer the business; schedule the consultants's time and allocate contracts to them; and bill clients and collect fees. At the beginning of the consulting year, the students received training sessions, held at each university, focusing on marketing the program, reporting procedures and quality of service.

The program has been running since 1972. USBC clients were surveyed in 1989 and 80% said they were satisfied with the service they received. Areas of concern among clients not satisfied with the service were failure

to reach a clear understanding of what was expected from the consultants and the consultants' lack of experience in assessing small-business problems. The students felt their expectations had been met by the program and gave it a high rating. Another survey of the program's clients was conducted late in 1990 to measure the effectiveness of the consulting service.

CHAPTER 9
PEOPLE AND SKILLS

In the past year, research has demonstrated a serious gap in the ability of Ontario to equip the people of this province with the training necessary to do their jobs adequately.

- The report of the Premier's Council on *People and Skills in the New Global Economy* delivered a strong criticism on the uncoordinated state of training services offered by the private sector and by the federal and provincial governments.

- Research by Small Business Ontario[1], buttressed by consultation with business owners, found that entrepreneurs lack critical skills to run their businesses. Chief among these are personnel management, finance, strategic planning and marketing, and intelligence on technological change. Prospective business owners echo this sentiment, although their needs are more strongly tilted towards market information, assistance available from governments and elsewhere, regulations that apply to their businesses and planning skills necessary to raise capital.

- The needs of business owners are intensified by the special needs of minority groups, including youth, women, the economically and physically disadvantaged, the aboriginal community and the ethno-cultural communities. These groups have business needs that have not traditionally been addressed in assistance designed to help small firms.

The shortage of skilled labour

Five years ago, about 62% of the employees in Ontario's auto parts industry were unskilled[2]. Today, 33% in that industry are unskilled. More than half the new jobs in Canada now require a grade 12 education or better; in another decade, this qualification will be adequate for only 37%

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[1]Source: Partners Conference Theme Papers. 1990

[2]Source: *People and Skills in the New Global Economy*, a report of the Premier's Council, 1990

of new jobs. Yet one third of Ontario's students drop out of school before they receive their diploma.

In its report on skills, the Premier's Council outlined a serious skills deficit for Ontarian industry. Matters seem likely to become worse, too, because enrolment in technical subjects at community colleges and universities is declining, while enrolment in academic and arts courses continues to rise. In industry, according to the Council, spending in Canada on employee training is half the spending in the U.S., and a quarter that of Germany's. One major problem identified by the Council was that there is little coordination among the many programs offered by both levels of government and by private firms, making access to quality training difficult for those seeking assistance.

This is somewhat unfair to Ontario's Ministry of Skills Development, which spends about $280 million a year on training. Despite some of the Council's criticisms, small firms give a high rating to the services offered by the Ontario Skills Development Offices (OSDOs). During 1989-90, this program assisted 13,000 clients, 94% of them with fewer than 200 employees. OSDOs assist clients to identify training and human resource development needs, to undertake training and to evaluate the success of the training offered. The program also refers clients to appropriate funding sources. One such program, Ontario Skills, funds 80% of the training costs for firms with fewer than 200 employees and 60% for bigger firms. The delivery of these subsidies is extremely flexible. Depending on the client's needs, the program can fund training at a college or on-the-job using staff trainers or external consultants. In 1989-90, this program helped 8,600 firms; 85,000 people were trained, half of them women.

The Premier's Council recommended the government establish an Ontario Training and Adjustment Board, that would be managed jointly by management and labour and would administer all training and adjustment needs in the province. When this report went to press, no action had yet been taken on this recommendation.

The needs of business owners

Despite the availability of significantly more and vastly better training tools for small business owners than existed only 10 years ago, entrepreneurs are generally slow to seek assistance. Small Business Ontario has identified a number of possible explanations for this: Some are unaware of the training possibilities available to them (see, for example, the study on Franco-Ontarian entrepreneurs in chapter 5); some cannot afford them; and some

lack the necessary prerequisites to profit from them (literacy skills etc). Another important reason is that they do not think they have the time to spend on improving their skills in this area. When business pressures are intense, it is not always easy to take off even an afternoon to contemplate a problem or an opportunity that does not have to be resolved that day.

There is, nonetheless, a dearth of expertise in small firms in personnel management, a dearth that is exaggerated because so few business owners appreciate the extent to which they need help. There is a gap, however, at two levels. First, the mounting shortage of skilled labour means that entrepreneurs need the ability to attract and retain employees with vital skills. Second, the pressure to increase productivity means that they need to find more and better ways to motivate their key employees.

To address this need, Small Business Ontario has experimented with innovative solutions. It mounted a pilot project in the spring of 1990 to offer three workshops on people management to business owners in Thunder Bay, Oakville and Kitchener-Waterloo. The workshops attempted to demonstrate that people management lies at the heart of any solution to competitiveness and that owners can control their futures in this regard through a series of proven techniques. Finally, the workshops showed how this can benefit the firm's profitability. The techniques to improve personnel management included such things as:

- Involving employees in setting goals;
- Creating an appropriate balance of incentives;
- Allowing employees to become shareholders;
- Reducing turnover and increasing productivity; and
- Improving the long-term return on investment in training.

The workshop in Thunder Bay was co-sponsored by the Northwest Enterprise Centre, while the other two were co-sponsored by the local chambers of commerce. The co-sponsors were primarily responsible for recruiting the participants. A total of 81 firms attended, almost half of which (45%) had fewer than 20 employees. A sixth (usually not owners) were in large firms with more than 100 employees and the balance of 40% owned firms with 20 to 99 employees.

Each workshop featured presentations by two small-business owners. These presentations were well received by participants. Reaction to the seminar as a whole, however, varied according to the participant's educational background, firm size and reason for attending. A number of the participants were in the target market for the workshop and they benefitted greatly from it; in one group, 62% said they had changed their management approach as a result of the workshop. Some, however, came with expectations that did not match the subject matter or the level of sophistication of the material, so they were disappointed. On average, however, three quarters of the participants said they were already good people managers.

There was a consensus that owner forums, where people matters could be discussed between them, would be desirable. Also, few appear willing to pay much more than a nominal fee for such a workshop. Most important of all, the workshop needs to be marketed with great clarity, to ensure the right kind of owners attend. In this regard the selection of co-sponsors is critical. In general, the response to government initiatives in the field of personnel management was favourable.

Technical Personnel Program

This program, introduced in 1989, is designed to raise the level of technical skills in smaller Ontario companies; to promote capital investment and accelerate the adoption of new technology; and to reduce manufacturing costs, increase productivity and improve export capability. The program is an initiative recommended by the Premier's Council, and funded by the Ontario Technology Fund, with a budget of $38 million over the five-year duration of the program.

The program pays 50% of the salary of a new technical employee in the first year of employment and 25% of the salary in the second year. The maximum contribution is $45,000. To qualify, companies must have 10-200 employees on a consolidated basis. They must also be exporters or have specific plans to become exporters, and need to hire a technical or scientific person in order to achieve that goal. They must have a specific project in mind. The program is administered in conjunction with the National Research Council, whose officers assess the technical merits of the projects, and the Ministry's field consultants, through whom applications must flow.

In its first year, TPP approved 206 applications (82%) for an average contribution of $33,000 on an average salary of $44,000. The industries that attracted the most interest were machinery and equipment and industrial

and consumer electronics, each of which accounted for almost a quarter of the applications approved. More than 40% of the applications were by companies with sales of less than $2 million and another 22% had sales of $2 million to $5 million.

Engineering personnel accounted for 79% of the new technical employees. Some of the benefits gained by hiring these people were improvements in productivity; more efficient manufacturing processes; formal quality control systems; the installation of CAD/CAM systems; and software development. TPP is enjoying positive feedback, particularly from firms which were able to hire their first engineer through the program. TPP commitments in its first year exceeded $5 million. Participating companies that were doing Research & Development committed almost $100,000 in R&D funds over three years.

APPENDIX: SMALL BUSINESS ADVOCACY REPORTS

These research reports are available from Small Business Advocacy, Ministry of Industry, Trade and Technology, 7th Floor, Hearst Block, 900 Bay Street, Toronto, Ontario M7A 2E1 (416) 965-6304.

1. **Survey of Small Business Registrants, 1984 (October 1984)**

   Results of interviewing 911 Ontario entrepreneurs about the businesses they start. Includes information on investment, hiring intent, previous experience, type of business, why the business was started and demographics.

2. **Self-Directed RRSP Investment in Private Companies (May 1985)**

   Survey of characteristics of holders of self-directed RRSP's (150 people). Results compared to information obtained from 2,000 people when they either opened self-directed RRSP's or transferred funds to such an RRSP. Survey was conducted on behalf of SBA by Decision Marketing Research Limited.

3. **Expanding Ontario's Small Business Development Corporations Program to Business Services (May 1985)**

   Argument for extending eligibility under Ontario's SBDC program to Ontario's business service firms. Also argues for expansion of SBDC's existing Match-up Service to introduce appropriate SBDC investors and small business owners and emphasize smaller placements of equity.

4. **An Advance Notice System for Proposed Regulatory Initiatives (September 1985)**

Proposal to create an Advance Notice System In Ontario. Includes an examination of advance notice in place in other jurisdictions, description of Ontario's history with respect to advance notice, identification of principles to be considered in any improvement of the regulatory process and policy options and recommendations.

5. **Newly-formed Small Businesses in Ontario, 1982-84 (August 1985)**

Results of interviewing 861 Ontario entrepreneurs. Provides a profile of Ontario's small business owners and their attitudes about various issues and programs, as well as a comparison of unincorporated and incorporated businesses. Additionally, the research provides a profile of the kinds of businesses that are started and remain viable. Survey was conducted on behalf of SBA by The Creative Research Group.

6. **Small Business Payroll Taxes (March 1986)**

The economic implications of payroll taxation on small businesses are examined. Also looks at the effects of abolishing Ontario Health Insurance Plan premium payments and replacing the payments with a 2% employer-paid payroll tax. Features an examination of impacts on an average small business, a garage, a restaurant, a construction firm and a manufacturer.

7. **Small Business Regulation and Paperburden (March 1986)**

A joint project of SBA and the Department of Regional Industrial Expansion, Ontario Region, the study identifies and clarifies specific areas of regulatory and paperburden in Ontario's small business community. Looks at problems and problem sources identified by the general economic sectors and more specifically the tourism sector. Survey was conducted by The DPA Group Incorporated.

8. **Entrepreneurship and Small Business (May 1986)**

A discussion paper tabled in Ontario Legislature by the Minister of Industry, Trade and Technology as a supplement to the Ontario Budget of April 1986. Describes: entrepreneurship in Ontario, new business formation and small firm performance.

9. **The Ontario Investment Network (April 1986)**

Describes the rationale for the establishment of the Ontario Investment Network (presently operated by the Chamber of Commerce under the name Canada Opportunities Investment Network - COIN). Discusses the chronic shortage of equity capital suffered by the small business community across Canada.

10. **New Small Businesses (April 1986)**

The 1986 survey of new unincorporated business starts. The results of 1,118 interviews show the age, sex, previous ownership and employment experience of new business owners as well as the reasons for starting the business. The study also breaks down the startups by sector and expected billings and source of investment.

11. **New Ventures: A Loan Guarantee Program for New Businesses in Ontario (June 1986)**

Describes the rationale for the New Ventures Program, announced in the Speech from the Throne in April 1986. Discusses access to financing problems of small businesses. Shows design of the New Ventures program including details on eligibility criteria, program administration, roles of co-sponsors, application processes and costs of program. A project of the Committee of Parliamentary Assistants for Small Business.

12 Small Business Capitalization and Proposed Pension Investment Reports (August 1986)

SBA submission to the Pension Commission of Ontario regarding the policy recommendations for the regulation of pension fund investments. Argues for expanding the universe of eligible pension fund investments to include more small businesses. Includes copy of the Pension Commission recommendations.

13. Targeting Employee Share Ownership Plans to Small Business (September 1986)

Describes the rationale for targeting the Employee Share Ownership Plans program (announced in the June 1986 Budget) to small businesses. Provides recommendations on how the plan's optimum use by the small business community may be encouraged.

14. Workers' Compensation Experience Rating - A Claim Deductible Concept (October 1986)

The study examines the feasibility of introducing the concept of claims deductibility in the experience rating of claims costs under Workers' Compensation in Ontario. Study was conducted on behalf of SBA by William M. Mercer Ltd.

15. Hours of Work and Overtime in Small Businesses: Five Case Studies (December 1986)

Case studies of hours of work and overtime practices in five Ontario firms: sewer and water main contracting, clothing manufacturer, courier and moving service, lumber and building supply and weigh scale repair and distribution. Qualitative research on attitudes of owners towards overtime and data on firms and their practices.

16. **The State of Small Business (December 1986)**

The first annual report on small business in Ontario. Features data on: the job creation record and growth of small business, profiles of the small business owner, franchising, women business owners, the aspirations and achievements of new business owners, small business financing and effects of public policy on the small business community. Tabled in the Ontario Legislature in December 1986 by the Minister of Industry, Trade and Technology.
Available in French as La Situation des petites enterprises.

17. **University Centres of Entrepreneurship for Ontario (February 1987)**

Describes rationale for the establishment of centres of entrepreneurship in Ontario universities. Included in the April 1986 Speech From The Throne.

18 **Ontario's Fast-Growth Companies (April 1987)**

Examines the characteristics of 84 successful Ontario entrepreneurs. Study conducted on behalf of SBA by Decision Marketing Research Limited.

19. **Small Business Payroll Taxes, 1987 (March 1987)**

The 1987 update f the 1986 Small Business Payroll Tax study. It focuses on the increasing burden Workers' Compensation places on small businesses.

20. **The Status of Female Employees in Small Business (June 1986)**

Survey of 353 owners of small manufacturing businesses in Ontario regarding the status of women in their firms. Examines employment patterns, wage and salary administration, personnel practices and company policies. Also looks at which form of pay equity legislation would least affect the viability of small businesses. Survey was conducted on behalf of SBA by Hay Management Consultants.

21. **Pay Equity and Ontario's Small Business Sector (June 1986)**

Survey of 302 Ontario small business owners regarding the types of personnel practices they follow in their firms. Also includes results of 16 interviews with persons knowledgeable about pay equity and small business regarding how to implement pay equity in small businesses. Survey conducted on behalf of SBA by Urban Dimensions Group, Inc.

22. **Business Transfer Tax: Modelling the Impact on Small Firms (November 1987)**

Study demonstrates how profits and sales in several Ontario small businesses might be affected by the federal government's proposed business transfer tax. Examines eight types of businesses: retail florists (unincorp. and incorp.), retail drug stores (incorp.), retail jewellery stores (incorp.), rubber processors and suppliers (incorp.), engineering processing firms (incorp.), and lodges and motels (incorp.).

23. **Business Starts in Ontario: An Econometric Analysis and Forecasting Model (August 1987)**

Reports on the determinants of new business starts, including changes in population and labour force, industrial structure and rates of unemployment output growth, costs of borrowing and inflation. Includes a computer-based forecasting model for the next five years. Study carried out by Quantec Research Ltd.

24. **Hours of Work and Overtime in Small Business (January 1988)**

Compares a sample of 300 small firms with control group of 60 large firms to assess the impact of recommendations proposed by the Task Force on Hours of Work and Overtime submitted in May 1987. Finds that the proposals are unlikely to have a significant effect on overall average hours worked per week in Ontario, but that some of the recommendations affect small and large firms differently. Small businesses are relatively more affected by proposals to shorten the regular work week from 44 to 40 hours.

25. **Facilitating the Investment of Self-Directed RRSP Funds in Small Businesses (July 1988)**

Examines 1986 amendments to the federal Income Tax Act permitting holders of Registered Retirement Savings Plans (RRSPs) to invest in small and developing businesses. Recommends simplifying the rules and shifting the burden of compliance from financial institutions to the involved parties. Contends that the changes will increase RRSP investments in small businesses.

26. **Safety Matters: Case Studies in Health and Safety Practices in the Workplace (September 1988)**

Case studies of 13 companies (of which six had fewer than 100 employees) examining the differences in approach between large, medium and small firms. Discloses that the larger the company, the more extensive its formal health and safety program. While larger companies have well-developed health and safety philosophies, small firms tend to do positive things in the workplace because the owners care about their employees' welfare and are sensitive to the disruption an accident can cause.

27. **Newly-Formed Small Businesses in Ontario, 1985-87 (August 1988)**

Based on interviews with 1,055 small firms, updates the August 1985 report on newly-formed small companies. Focuses on management, operational and policy issues for both incorporated and unincorporated firms. Efforts were made to increase the sample size of companies having more than 20 employees in order to better understand the phenomenon of growth. Discloses that finding and keeping qualified employees is now the top-rated barrier facing young companies.

28. Employment Standards in Small Firms (March 1988)

By a telephone survey of 307 small Ontario businesses and a control group of 25 larger firms, examines employee compensation issues, including possible changes to the minimum wage, training, benefits, vacations and leave arrangement, subcontracting and contracting out, and retirement policies.

29. An Equity Financing Vehicle for Growth Companies (January 1989)

Discusses a possible Ontario investment vehicle to improve the equity financing of companies with growth potential. Applies the U.S. model of small business investment companies, under which the government guarantees debentures issued by investment companies that specialize in small business. This approach, successfully practised in the U.S. since 1958, was responsible for the genesis of much of the American venture capital industry. It enabled venture capital firms to multiply their capital under management and operate at a scale sufficient to build up the investment, management, and marketing expertise necessary to manage a portfolio of growing firms.

30. The State of Small Business, 1987 (December 1987)

The second annual report on small business in Ontario. Features the Committee of Parliamentary Assistants for Small Business' proposal for a small business impact statement (SBIS) to set out in cabinet submissions the impact on the small business community of proposed changes in Ontario policy, legislation and regulations. Concentrates on the dynamic growth of small businesses in Ontario and includes research findings on where the jobs are coming from, the performance of successful young companies, remaining barriers to growth and the government's response.

31. Survey of Student Attitudes on Entrepreneurship and Small Business (September 1989)

Survey of 929 students in Grades 7 & 8 and Grades 11 & 12 examines student attitudes on entrepreneurship and small business. The survey was conducted among students in Thunder Bay and East York. It investigates students' awareness and knowledge of small business, perceptions of small business owners and the likelihood of starting their own business in the future. Environics Research Group Limited analyzed the data.

32. The State of Small Business, 1988 (January 1989)

The third annual report on small business in Ontario. Features a bilingual small business owners guide as well as data on job creation. Concentrates on growth opportunities with specific reference to exporting, high technology, and government procurement. Small business financing is also highlighted.

33. Report on the Evaluation of the New Ventures Program (March 1989)

Review of Ontario's New Ventures Program by Price Waterhouse. New Ventures has assisted more than 13,000 new businesses in accessing over $160,000,000 in private sector financing during the past three years. The analysis outlines user and lender profiles, the program's costs and benefits as well as projections for future costs.

34. Business Ownership for Women (BOW) Review (August 1989)

Review by Ivy Lea Consultants of the Ministry's BOW Program. The program, which comprised 50 seminars and seven conferences, ran from September 1985 to 1988. The report assesses the effectiveness of the program and recommends future government programming in support of women entrepreneurs.

35. University Small Business Consulting (USBC) Review (October 1989)

Review by the DPA Group Inc. of the Ministry's USBC Program. The USBC program offers low cost student consulting services to local small businesses. The service is provided from May to the end of August each year at 15 Ontario universities. The review assesses the effectiveness and value of the program.

36. Managing People in Small Business (August 1989)

Report of six focus groups conducted with small business owners and those involved in managing people. Its purpose was to explore initiatives that MITT might undertake to improve people management in Ontario's small businesses. The conclusion was that there is a need for a well-developed multi-faceted program with direction proactive marketing.

37. Community Consultations on Employee Training in Small Business (June 1989)

This report of the Committee of Parliamentary Assistants for Small Business to the Minister of Skills Development contains findings of a seven-city tour by the Committee to investigate employee training in small business. It found that the Ontario Skills Development Offices in community colleges were an effective delivery vehicle of training services to small firms, though not enough business owners knew about programs of assistance.

38. Study on Franco-Ontarian Small Businesses (June 1990)

Telephone survey by Rhéal Leroux et Associés during 1989-90. This was a first look at this group of business persons. It covered such areas as: business sector, type, age, number of employees, annual revenues, use of government programs, use of the French language as well as the demographics of owners.

39. **Small Business Payroll Taxes, 1989-90 (July 1990)**

An update of earlier reports, this report indicates the impact of the changes made to Canada Pension Plan, Unemployment Insurance, Workers' Compensation Board premiums and the addition of the Employer Health Tax. Payroll taxes averaged $2,258 per small business worker in 1990, 8.7% of the average wage.

40. **The State of Small Business, 1989 (March 1990)**

The fourth annual report on small business in Ontario features an in-depth analysis of the motivations of entrepreneurs and a view of the self-employed, as well as updating data on job creation and business growth. The report examines how business expansion is financed, considering both public and private sources of capital.

41. **Small Business Payroll Taxes, 1990-91 (October 1990)**

An update of the 1989-90 report, this study forecasts the impact of payroll taxes on small firms in 1991. The increase is expected to slow in 1991 as most workers' compensation rates will not change.

42. **Survey of Family-owned Business (January 1991)**

This study combined a mail-out survey with administrative data provided by Statistics Canada. It yields an interesting view of a large segment of Ontario's businesses. More than half of the sample represented the first generation of the business and just under half of the family businesses are in the service sector.

Ontario

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